SIFCO INDUSTRIES INC
Form 10-Q
May 10, 2013

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, 2013

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 1-5978

SIFCO Industries, Inc.

(Exact name of registrant as specified in its charter)

Ohio	**34-0553950**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**
970 East 64th Street, Cleveland Ohio	**44103**
(Address of principal executive offices)	**(Zip Code)**

(216) 881-8600

(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. Yes x 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 x 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 definition of large accelerated filer , accelerated filer , non-accelerated filer , and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	¨	Accelerated filer	¨
Non-accelerated filer	¨	Smaller reporting company	x

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

The number of the Registrant s Common Shares outstanding at March 31, 2013 was 5,373,526.

Part I. **Financial Information**

Item 1. **Financial Statements**

SIFCO Industries, Inc. and Subsidiaries

Consolidated Condensed Statements of Operations

(Unaudited)

(Amounts in thousands, except per share data)

	Three Months Ended March 31, 2013	Three Months Ended March 31, 2012	Six Months Ended March 31, 2013	Six Months Ended March 31, 2012
Net sales	**$ 29,594**	$ 30,143	**$ 58,294**	$ 54,869
Cost of goods sold	**23,881**	24,344	**46,896**	44,284
Gross margin	**5,713**	5,799	**11,398**	10,585
Selling, general and administrative expenses	**3,258**	2,885	**7,062**	5,681
Amortization of intangible assets	**493**	662	**1,052**	1,477
Loss (gain) on disposal of operating assets	**3**	0	**(122)**	0
Operating income	**1,959**	2,252	**3,406**	3,427
Interest income	**(9)**	(4)	**(14)**	(8)
Interest expense	**79**	134	**185**	228
Foreign currency exchange (gain) loss, net	**(7)**	10	**0**	(3)
Other income, net	**(109)**	(117)	**(186)**	(234)
Income from continuing operations before income tax provision	**2,005**	2,229	**3,421**	3,444
Income tax provision	**536**	777	**1,031**	1,159
Income from continuing operations	**1,469**	1,452	**2,390**	2,285
Income (loss) from discontinued operations, net of tax	**(34)**	272	**2,460**	625
Net income	**$ 1,435**	$ 1,724	**$ 4,850**	$ 2,910
Income per share from continuing operations				
Basic	**$ 0.27**	$ 0.27	**$ 0.45**	0.43
Diluted	**$ 0.27**	$ 0.27	**0.44**	0.43
Income (loss) per share from discontinued operations, net of tax				
Basic	**$ (0.01)**	$ 0.05	**$ 0.46**	0.12
Diluted	**$ (0.01)**	$ 0.05	**$ 0.46**	0.12
Net income per share				
Basic	**$ 0.27**	$ 0.32	**$ 0.91**	0.55
Diluted	**$ 0.27**	$ 0.32	**$ 0.90**	0.55
Weighted-average number of common shares (basic)	**5,364**	5,315	**5,353**	5,303
Weighted-average number of common shares (diluted)	**5,404**	5,336	**5,398**	5,326

See notes to unaudited consolidated condensed financial statements.

SIFCO Industries, Inc. and Subsidiaries

Consolidated Condensed Statements of Comprehensive Income

(Unaudited)

(Amounts in thousands, except per share data)

	Three Months Ended March 31,		Six Months Ended March 31,	
	2013	**2012**	**2013**	**2012**
Net income	**$ 1,435**	$ 1,724	**$ 4,850**	$ 2,910
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustment	**(1)**	83	**(285)**	38
Net retirement plan liability adjustment	**329**	223	**558**	425
Interest rate swap agreement adjustment	**14**	(7)	**30**	(52)
Comprehensive income	**$ 1,777**	$ 2,023	**$ 5,153**	$ 3,321

See notes to unaudited consolidated condensed financial statements.

SIFCO Industries, Inc. and Subsidiaries

Consolidated Condensed Balance Sheets

(Amounts in thousands, except per share data)

	March 31, 2013 (unaudited)	September 30, 2012
ASSETS		
Current assets:		
Cash and cash equivalents	**$ 5,644**	$ 7,176
Receivables, net of allowance for doubtful accounts of $563 and $539, respectively	**22,531**	20,780
Inventories, net	**19,987**	17,505
Deferred income taxes	**1,343**	1,415
Prepaid expenses and other current assets	**1,730**	1,122
Current assets of business held for sale	**0**	3,908
Total current assets	**51,235**	51,906
Property, plant and equipment, net	**29,570**	29,726
Intangible assets, net	**13,575**	14,627
Goodwill	**7,015**	7,015
Other assets	**1,708**	695
Noncurrent assets of business held for sale	**0**	2,576
Total assets	**$ 103,103**	$ 106,545
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Current maturities of long-term debt	**$ 4,368**	$ 2,000
Accounts payable	**9,056**	9,181
Accrued liabilities	**5,988**	4,330
Current liabilities of business held for sale	**0**	1,171
Total current liabilities	**19,412**	16,682
Long-term debt, net of current maturities	**10,089**	19,683
Deferred income taxes	**293**	1,154
Other long-term liabilities	**7,984**	8,494
Noncurrent liabilities of business held for sale	**0**	390
Shareholders equity:		
Serial preferred shares, no par value, authorized 1,000 shares	**0**	0
Common shares, par value $1 per share, authorized 10,000 shares; issued and outstanding shares 5,407 at March 31, 2013 and 5,366 at September 30, 2012	**5,407**	5,366
Additional paid-in capital	**7,512**	7,523
Retained earnings	**64,447**	59,597
Accumulated other comprehensive loss	**(12,041)**	(12,344)
Total shareholders equity	**65,325**	60,142
Total liabilities and shareholders equity	**$ 103,103**	$ 106,545

See notes to unaudited consolidated condensed financial statements.

SIFCO Industries, Inc. and Subsidiaries

Consolidated Condensed Statements of Cash Flows

(Unaudited)

(Amounts in thousands)

	Six Months Ended March 31, 2013	2012
Cash flows from operating activities:		
Net income	**$ 4,850**	$ 2,910
Income from discontinued operations, net of tax	**(2,460)**	(625)
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	**2,987**	3,104
Gain on disposal of operating assets	**(122)**	0
LIFO expense (income)	**(407)**	428
Share transactions under company stock plan	**30**	498
Deferred income taxes	**(10)**	81
Changes in operating assets and liabilities:		
Receivables	**(1,751)**	1,016
Inventories	**(2,076)**	(4,433)
Refundable income taxes	**0**	243
Prepaid expenses and other current assets	**(607)**	(388)
Other assets	**(1,013)**	(203)
Accounts payable	**(125)**	856
Accrued liabilities	**645**	170
Other long-term liabilities	**100**	(22)
Net cash provided by operating activities of continuing operations	**41**	3,635
Net cash provided by (used for) operating activities of discontinued operations	**(235)**	483
Cash flows from investing activities:		
Acquisition of business	**0**	(24,721)
Proceeds from disposal of operating assets	**125**	0
Capital expenditures	**(1,782)**	(1,169)
Net cash used for investing activities of continuing operations	**(1,657)**	(25,890)
Net cash provided by (used for) investing activities of discontinued operations	**8,641**	(93)
Cash flows from financing activities:		
Proceeds from term note	**0**	10,000
Repayments of term note	**(1,000)**	(1,000)
Proceeds from revolving credit agreement	**26,725**	37,016
Repayments of revolving credit agreement	**(32,974)**	(24,812)
Proceeds from other debt	**0**	2,302
Dividends paid	**(1,073)**	(1,060)
Other	**0**	(28)
Net cash provided by (used for) financing activities of continuing operations	**(8,322)**	22,418
Increase (decrease) in cash and cash equivalents	**(1,532)**	553
Cash and cash equivalents at the beginning of the period	**7,176**	6,431
Effect of exchange rate changes on cash and cash equivalents	**0**	25
Cash and cash equivalents at the end of the period	**$ 5,644**	$ 7,009

Supplemental disclosure of cash flow information of continuing operations:		
Cash paid for interest	**$ (172)**	$ (201)
Cash paid for income taxes, net	**(2,241)**	(1,159)

See notes to unaudited consolidated condensed financial statements.

SIFCO Industries, Inc. and Subsidiaries

Notes to Unaudited Consolidated Condensed Financial Statements

(Amounts in thousands, except per share data)

1. Summary of Significant Accounting Policies

A. Principles of Consolidation

The accompanying unaudited consolidated condensed financial statements include the accounts of SIFCO Industries, Inc. and its wholly-owned subsidiaries (the Company). All significant intercompany accounts and transactions have been eliminated.

The U.S. dollar is the functional currency for all of the Company s U.S. operations and its Irish subsidiary. For these operations, all gains and losses from completed currency transactions are included in income currently. Foreign currency translation adjustments are reported as a component of accumulated other comprehensive loss in the unaudited consolidated condensed financial statements.

These unaudited consolidated condensed financial statements should be read in conjunction with the consolidated financial statements and related notes included in the Company s fiscal 2012 Annual Report on Form 10-K. The results of operations for any interim period are not necessarily indicative of the results to be expected for other interim periods or the full year.

B. Net Income per Share

The Company s net income per basic share has been computed based on the weighted-average number of common shares outstanding. Net income per diluted share reflects the effect of the Company s outstanding stock options, restricted shares and performance shares under the treasury stock method. The dilutive effect of the Company s stock options, restricted shares and performance shares were as follows:

	Three Months Ended March 31,		Six Months Ended March 31,	
	2013	**2012**	**2013**	**2012**
Income from continuing operations	**$ 1,469**	$ 1,452	**$ 2,390**	$ 2,285
Income (loss) from discontinued operations, net of tax	**(34)**	272	**2,460**	625
Net income	**$ 1,435**	$ 1,724	**$ 4,850**	$ 2,910
Weighted-average common shares outstanding (basic)	**5,364**	5,315	**5,353**	5,303
Effect of dilutive securities:				
Stock options	**1**	20	**1**	22
Restricted shares	**9**	1	**8**	1
Performance shares	**30**	0	**36**	0
Weighted-average common shares outstanding (diluted)	**5,404**	5,336	**5,398**	5,326
Net income per share basic				
Continuing operations	**$ 0.27**	$ 0.27	**$ 0.45**	$ 0.43
Discontinued operations	**(0.01)**	0.05	**0.46**	0.12
Net income	**$ 0.27**	$ 0.32	**$ 0.91**	$ 0.55
Net income per share diluted:				
Continuing operations	**$ 0.27**	$ 0.27	**$ 0.44**	$ 0.43
Discontinued operations	**(0.01)**	0.05	**0.46**	0.12

Net income	**$ 0.27**	$ 0.32	**$ 0.90**	$ 0.55
Anti-dilutive weighted-average common shares excluded from calculation of diluted earnings per share	**51**	151	**78**	147

C. Derivative Financial Instruments

The Company uses an interest rate swap agreement to reduce risk related to variable-rate debt, which is subject to changes in market rates of interest. The interest rate swap is designated as a cash flow hedge. At March 31, 2013, the Company held one interest rate swap agreement with a notional amount of $7,000. Cash flows related to the interest rate swap agreement are included in interest expense. The Company s interest rate swap agreement and its variable-rate term debt are based upon LIBOR. During the first six months of fiscal year 2013, the Company s interest rate swap agreement qualified as a fully effective cash flow hedge against the Company s variable-rate term note interest risk.

D. Impact of Newly Issued Accounting Standards

In February 2013, the Financial Accounting Standards Board issued Accounting Standards Update (ASU) 2013-02, Comprehensive Income , which provides guidance on disclosure requirements for items reclassified out of Accumulated Other Comprehensive Income (AOCI). This new guidance requires entities to present (either on the face of the income statement or in the notes to the financial statements) the effects on the income statement of amounts reclassified out of AOCI. The new guidance will be effective for the Company beginning October 1, 2013. The Company does not expect the adoption of this ASU to have a material impact on its consolidated financial statements.

In March 2013, the Financial Accounting Standards Board issued ASU 2013-05, Foreign Currency Matters , which provides guidance on a parent s accounting for the cumulative translation adjustment upon derecognition of a subsidiary or group of assets within a foreign entity. This new guidance requires that the parent release any related cumulative translation adjustment into net income only if the sale or transfer results in the complete or substantially complete liquidation of the foreign entity in which the subsidiary or group of assets had resided. The new guidance will be effective for the Company beginning October 1, 2014. The adoption of this guidance is not expected to have a material impact on the Company s consolidated financial statements.

E. Reclassifications

Certain prior period amounts were reclassified to conform to the current consolidated financial statement presentation.

2. Inventories

Inventories consist of:

	March 31, 2013	September 30, 2012
Raw materials and supplies	**$ 7,112**	$ 4,207
Work-in-process	**7,352**	9,156
Finished goods	**5,523**	4,142
Total inventories	**$ 19,987**	$ 17,505

Inventories are stated at the lower of cost or market. Cost is determined using the last-in, first-out (LIFO) method for 37% and 44% of the Company s inventories at March 31, 2013 and September 30, 2012, respectively. The first-in, first-out (FIFO) method is used for the remainder of the inventories. If the FIFO method had been used for the inventories for which cost is determined using the LIFO method, inventories would have been $9,130 and $9,537 higher than reported at March 31, 2013 and September 30, 2012, respectively.

3. Goodwill and Intangible Assets

The Company s intangible assets by major asset class subject to amortization consist of:

March 31, 2013	Estimated Useful Life	Original Cost	Accumulated Amortization	Net Book Value
Intangible assets:				
Trade name	**10 years**	**$ 1,900**	**$ 349**	**$ 1,551**
Non-compete agreement	**5 years**	**1,500**	**514**	**986**
Below market lease	**5 years**	**900**	**415**	**485**
Customer relationships	**10 years**	**13,000**	**2,447**	**10,553**
Order backlog	**1 year**	**2,100**	**2,100**	**0**
Total intangible assets		**$ 19,400**	**$ 5,825**	**$ 13,575**

September 30, 2012	Estimated Useful Life	Original Cost	Accumulated Amortization	Net Book Value
Intangible assets:				
Trade name	10 years	$ 1,900	$ 254	$ 1,646
Non-compete agreement	5 years	1,500	364	1,136
Below market lease	5 years	900	325	575
Customer relationships	10 years	13,000	1,796	11,204
Order backlog	1 year	2,100	2,034	66
Total intangible assets		$ 19,400	$ 4,773	$ 14,627

The amortization expense on identifiable intangible assets for the six months ended March 31, 2013 and 2012 was $1,052 and $1,477, respectively. Amortization expense associated with the identified intangible assets, all of which relates to the Forged Components Group, is expected to be as follows:

	Amortization Expense
Fiscal year 2013	$ 2,037
Fiscal year 2014	1,970
Fiscal year 2015	1,970
Fiscal year 2016	1,744
Fiscal year 2017	1,507

The Company s goodwill, all of which relates to the Forged Components Group, is not being amortized and is subject to annual impairment tests. All of the goodwill is expected to be deductible for tax purposes.

4. Accumulated Other Comprehensive Loss

The components of accumulated other comprehensive loss are as follows:

	March 31, 2013	September 30, 2012
Foreign currency translation adjustment, net of tax	**$ (5,851)**	$ (5,566)
Net retirement plan liability adjustment, net of tax	**(6,162)**	(6,720)

Interest rate swap agreement adjustment, net of tax	**(28)**	(58)
Total accumulated other comprehensive loss	**$ (12,041)**	$ (12,344)

5. Long-Term Debt

Long-term debt consists of:

	March 31, 2013	September 30, 2012
Revolving credit agreement	**$ 5,089**	$ 11,338
Term loan	**7,000**	8,000
Promissory Note	**2,368**	2,345
	14,457	21,683
Less current maturities	**4,368**	2,000
Total long-term debt	**$ 10,089**	$ 19,683

In October 2011, the Company entered into an amendment to its existing credit agreement (the Credit Agreement Amendment) with its bank increasing the maximum borrowing amount from $30,000 to $40,000, of which $10,000 is a five (5) year term loan and $30,000 is a five (5) year revolving loan, secured by substantially all the assets of the Company and its U.S. subsidiaries and a pledge of 65% of the stock of its Irish subsidiary. The term loan is repayable in quarterly installments of $500 starting December 1, 2011.

The term loan has a Libor-based variable interest rate that was 2.20% at March 31, 2013. This rate becomes an effective fixed rate of 2.90% after giving effect to an interest rate swap agreement.

Borrowing under the revolving loan bears interest at a rate equal to Libor plus 0.75% to 1.75%, which percentage fluctuates based on the Company s leverage ratio of outstanding indebtedness to EBITDA. At March 31, 2013, the interest rate was 1.00%. The loans are subject to certain customary financial covenants including, without limitation, covenants that require the Company to not exceed a maximum leverage ratio and to maintain a minimum fixed charge coverage ratio. There is also a commitment fee ranging from 0.10% to 0.25% to be incurred on the unused balance. The Company was in compliance with all applicable loan covenants as of March 31, 2013.

In connection with the purchase of the forging business and substantially all related operating assets from GEL Industries, Inc. (DBA Quality Aluminum Forge, Inc.) (QAF), as discussed more fully in Note 10, the Company issued a non-interest bearing promissory note to the seller, which note is payable by the Company in November, 2013. The imputed interest rate used to discount the note was 2.00% per annum.

6. Income Taxes

For each interim reporting period, the Company makes an estimate of the effective tax rate it expects to be applicable for the full fiscal year for its continuing operations. This estimated effective rate is used in providing for income taxes on a year-to-date basis. The Company s effective tax rate through the first six months of fiscal 2013 is 30%, compared to 34% for the same period of fiscal 2012, and differs from the U.S. federal statutory rate due primarily to (i) the impact of U.S. state and local income taxes, (ii) a domestic production activities deduction, (iii) application of tax credits, and (iv) the recognition of U.S. federal income taxes on undistributed earnings of non-U.S. subsidiaries.

The income tax provision consists of the following:

	Three Months Ended March 31,		Six Months Ended March 31,	
	2013	**2012**	**2013**	**2012**
Current income tax provision:				
U.S. federal	**$ 418**			