

EXPEDITORS INTERNATIONAL OF WASHINGTON INC
Form 10-Q
August 06, 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 June 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, 12thFloor, Seattle, Washington 98104
(Address of principal executive offices) (Zip Code)
(206) 674-3400
(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 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 August 3, 2015, the number of shares outstanding of the issuer's Common Stock was 189,159,975.

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)

	June 30, 2015	December 31, 2014
Current Assets:		
Cash and cash equivalents	\$985,727	\$927,107
Short-term investments	47,047	40,336
Accounts receivable, less allowance for doubtful accounts of \$7,369 at June 30, 2015 and \$7,119 at December 31, 2014	1,194,180	1,236,042
Deferred Federal and state income taxes	20,930	20,279
Other	86,871	65,486
Total current assets	2,334,755	2,289,250
Property and equipment, less accumulated depreciation and amortization of \$381,393 at June 30, 2015 and \$371,756 at December 31, 2014	536,121	538,415
Goodwill	7,927	7,927
Other assets, net	53,572	55,313
Total assets	\$2,932,375	\$2,890,905
Current Liabilities:		
Accounts payable	738,323	770,238
Accrued expenses, primarily salaries and related costs	228,537	192,468
Federal, state and foreign income taxes	26,821	21,077
Total current liabilities	993,681	983,783
Deferred Federal and state income taxes	48,961	35,514
Commitments and contingencies		
Shareholders' Equity:		
Preferred stock, none issued	—	—
Common stock, par value \$0.01 per share. Issued and outstanding 189,117,916 shares at June 30, 2015 and 191,655,690 shares at December 31, 2014	1,891	1,916
Additional paid-in capital	2,349	1,113
Retained earnings	1,935,159	1,903,196
Accumulated other comprehensive loss	(52,778)	(37,817)
Total shareholders' equity	1,886,621	1,868,408
Noncontrolling interest	3,112	3,200
Total equity	1,889,733	1,871,608
Total liabilities and equity	\$2,932,375	\$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		Six months ended	
	June 30,		June 30,	
	2015	2014	2015	2014
Revenues:				
Airfreight services	\$693,812	\$667,257	\$1,401,256	\$1,314,395
Ocean freight and ocean services	576,772	536,438	1,142,489	1,005,662
Customs brokerage and other services	420,969	395,446	825,334	770,729
Total revenues	1,691,553	1,599,141	3,369,079	3,090,786
Operating Expenses:				
Airfreight services	506,988	503,213	1,019,989	986,095
Ocean freight and ocean services	433,356	423,716	878,812	791,091
Customs brokerage and other services	199,068	187,498	388,651	364,300
Salaries and related costs	287,065	260,767	565,943	516,709
Rent and occupancy costs	24,971	25,401	50,359	50,563
Depreciation and amortization	11,420	12,417	22,949	24,799
Selling and promotion	10,529	9,291	19,776	17,464
Other	35,440	34,395	71,001	62,119
Total operating expenses	1,508,837	1,456,698	3,017,480	2,813,140
Operating income	182,716	142,443	351,599	277,646
Other Income (Expense):				
Interest income	2,636	2,764	5,368	5,461
Other, net	3,804	3,190	3,838	2,909
Other income, net	6,440	5,954	9,206	8,370
Earnings before income taxes	189,156	148,397	360,805	286,016
Income tax expense	70,827	56,669	135,144	110,093
Net earnings	118,329	91,728	225,661	175,923
Less net earnings attributable to the noncontrolling interest	569	426	1,197	797
Net earnings attributable to shareholders	\$117,760	\$91,302	\$224,464	\$175,126
Diluted earnings attributable to shareholders per share	\$0.61	\$0.46	\$1.17	\$0.88
Basic earnings attributable to shareholders per share	\$0.62	\$0.46	\$1.17	\$0.88
Dividends declared and paid per common share	\$0.36	\$0.32	\$0.36	\$0.32
Weighted average diluted shares outstanding	191,917,973	197,126,243	192,425,521	199,482,932
Weighted average basic shares outstanding	190,679,008	196,451,912	191,150,758	198,772,260

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		Six months ended	
	June 30, 2015	2014	June 30, 2015	2014
Net earnings	\$ 118,329	\$ 91,728	\$ 225,661	\$ 175,923
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments, net of tax of \$2,363 and \$2,723 for the three months ended June 30, 2015 and 2014 and \$8,197 and \$1,394 for the six months ended June 30, 2015 and 2014	4,216	4,985	(15,389)	2,608
Reclassification adjustment for foreign currency realized losses, net of tax of \$61 for the three and six months ended June 30, 2014	—	111	—	111
Other comprehensive income (loss)	4,216	5,096	(15,389)	2,719
Comprehensive income	122,545	96,824	210,272	178,642
Less comprehensive income attributable to the noncontrolling interest	472	440	769	860
Comprehensive income attributable to shareholders	\$ 122,073	\$ 96,384	\$ 209,503	\$ 177,782

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		Six months ended	
	June 30,		June 30,	
	2015	2014	2015	2014
Operating Activities:				
Net earnings	\$ 118,329	\$ 91,728	\$ 225,661	\$ 175,923
Adjustments to reconcile net earnings to net cash from operating activities:				
Provision for losses (recoveries) on accounts receivable	584	496	861	(619)
Deferred income tax expense	8,986	2,891	20,923	10,085
Excess tax benefits from stock plans	(366)	(495)	(1,846)	(984)
Stock compensation expense	11,663	11,877	21,570	22,171
Depreciation and amortization	11,420	12,417	22,949	24,799
Other	27	68	113	206
Changes in operating assets and liabilities:				
Decrease (increase) in accounts receivable	63,234	(84,618)	16,444	(72,390)
Increase in accounts payable and accrued expenses	8,038	61,377	22,933	90,923
Decrease in income taxes payable, net	(39,000)	(47,370)	(15,868)	(29,165)
(Increase) decrease in other current assets	(1,187)	(3,485)	2,382	(2,206)
Net cash from operating activities	181,728	44,886	316,122	218,743
Investing Activities:				
Purchase of short-term investments	(46,986)	(15,301)	(47,008)	(96,431)
Proceeds from maturities of short-term investments	—	15,643	40,296	36,619
Purchase of property and equipment	(12,912)	(9,635)	(22,357)	(18,395)
Escrow deposit for land acquisition	—	(27,101)	—	(27,101)
Other, net	(14)	(1,536)	184	134
Net cash from investing activities	(59,912)	(37,930)	(28,885)	(105,174)
Financing Activities:				
Proceeds from issuance of common stock	25,047	22,125	60,095	30,017
Repurchases of common stock	(128,137)	(131,391)	(205,505)	(358,116)
Excess tax benefits from stock plans	366	495	1,846	984
Dividends paid	(68,781)	(62,807)	(68,781)	(62,807)
Distributions to noncontrolling interest	—	—	(857)	(85)
Net cash from financing activities	(171,505)	(171,578)	(213,202)	(390,007)
Effect of exchange rate changes on cash and cash equivalents	2,272	4,137	(15,415)	(653)
(Decrease) increase in cash and cash equivalents	(47,417)	(160,485)	58,620	(277,091)
Cash and cash equivalents at beginning of period	1,033,144	1,131,046	927,107	1,247,652
Cash and cash equivalents at end of period	\$ 985,727	\$ 970,561	\$ 985,727	\$ 970,561
Taxes Paid:				
Income taxes	\$ 101,389	\$ 105,963	\$ 129,650	\$ 133,459

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 \$7,369 as of June 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.

6

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 six months ended June 30, 2015 and 2014, 2,919,750 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 none were issued in the six-month periods ended June 30, 2015 and 2014. In the second quarter of 2015 and 2014, respectively, 33,868 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:

	Six months ended June 30,			
	2015		2014	
Dividend yield	1.60	%	1.50	%
Volatility - stock option plans	31	%	36	%
Risk free interest rates	1.79	%	2.27	%
Expected life (years) - stock option plans	6.41 - 7.47		6.52 - 7.43	
Weighted average fair value of stock options granted during the period	\$13.42		\$14.08	

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

	Three months ended		Six months ended	
	June 30,		June 30,	
	2015	2014	2015	2014
Stock compensation expense	\$11,663	\$11,877	\$21,570	\$22,171
Recognized tax benefit	\$1,491	\$1,183	\$2,734	\$2,126

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		
	June 30, Net earnings attributable to shareholders	Weighted average shares	Earnings per share
2015			
Basic earnings attributable to shareholders	\$117,760	190,679,008	\$ 0.62
Effect of dilutive potential common shares	—	1,238,965	—
Diluted earnings attributable to shareholders	\$117,760	191,917,973	\$ 0.61
2014			
Basic earnings attributable to shareholders	\$91,302	196,451,912	\$ 0.46
Effect of dilutive potential common shares	—	674,331	—
Diluted earnings attributable to shareholders	\$91,302	197,126,243	\$ 0.46

(Amounts in thousands, except share and per share amounts)	Six months ended		
	June 30, Net earnings attributable to shareholders	Weighted average shares	Earnings per share
2015			
Basic earnings attributable to shareholders	\$224,464	191,150,758	\$ 1.17
Effect of dilutive potential common shares	—	1,274,763	—
Diluted earnings attributable to shareholders	\$224,464	192,425,521	\$ 1.17
2014			
Basic earnings attributable to shareholders	\$175,126	198,772,260	\$ 0.88
Effect of dilutive potential common shares	—	710,672	—
Diluted earnings attributable to shareholders	\$175,126	199,482,932	\$ 0.88

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

Shares	Three months ended		Six months ended	
	June 30, 2015	2014	June 30, 2015	2014
	8,406,717	15,633,365	10,519,482	16,778,917

Note 4. Components of Equity

The components of equity for the six months ended June 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	60,095	—	60,095
Shares repurchased under provisions of stock repurchase plans	(205,505)	—	(205,505)
Stock compensation expense	21,570	—	21,570
Tax benefits from stock plans, net	1,331	—	1,331
Net earnings	224,464	1,197	225,661
Other comprehensive loss	(14,961)	(428)	(15,389)
Dividends paid (\$0.36 per share)	(68,781)	—	