TreeHouse Foods, Inc.
Form 10-Q
November 04, 2011
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark One)

x **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities and Exchange Act of 1934**
For the Quarterly Period Ended September 30, 2011.

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 001-32504

TreeHouse Foods, Inc.

(Exact name of the registrant as specified in its charter)

Delaware	**20-2311383**
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification no.)
2021 Spring Road, Suite 600	
Oak Brook, IL	**60523**
(Address of principal executive offices)	(Zip Code)

(Registrant s telephone number, including area code) **(708) 483-1300**

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 the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer	x	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 x

Number of shares of Common Stock, $0.01 par value, outstanding as of October 21, 2011: 35,910,797

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Part I Financial Information

Item 1. Financial Statements

TREEHOUSE FOODS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except per share data)

	September 30, 2011 (Unaudited)	December 31, 2010
Assets		
Current assets:		
Cash and cash equivalents	$ 3,080	$ 6,323
Receivables, net	147,938	126,644
Inventories, net	367,446	287,395
Deferred income taxes	992	3,499
Prepaid expenses and other current assets	14,872	12,861
Assets held for sale	4,081	4,081
Total current assets	538,409	440,803
Property, plant and equipment, net	400,419	386,191
Goodwill, net	1,069,856	1,076,321
Intangible assets, net	443,633	463,617
Other assets, net	23,743	24,316
Total assets	$ 2,476,060	$ 2,391,248
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable and accrued expenses	$ 201,978	$ 202,384
Current portion of long-term debt	2,241	976
Total current liabilities	204,219	203,360
Long-term debt	990,474	976,452
Deferred income taxes	197,496	194,917
Other long-term liabilities	43,261	38,553
Total liabilities	1,435,450	1,413,282
Commitments and contingencies (Note 17)		
Stockholders equity:		
Preferred stock, par value $0.01 per share, 10,000 shares authorized, none issued		
Common stock, par value $0.01 per share, 90,000 shares authorized, 35,904 and 35,440 shares issued and outstanding, respectively	359	354
Additional paid-in capital	711,388	703,465
Retained earnings	350,723	286,181
Accumulated other comprehensive loss	(21,860)	(12,034)
Total stockholders equity	1,040,610	977,966
Total liabilities and stockholders equity	$ 2,476,060	$ 2,391,248

See Notes to Condensed Consolidated Financial Statements.

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TREEHOUSE FOODS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(In thousands, except per share data)

	Three Months Ended September 30, 2011	Three Months Ended September 30, 2010	Nine Months Ended September 30, 2011	Nine Months Ended September 30, 2010
	(Unaudited)		(Unaudited)	
Net sales	$ 528,050	$ 464,242	$ 1,514,183	$ 1,307,561
Cost of sales	402,518	354,005	1,158,285	1,002,396
Gross profit	125,532	110,237	355,898	305,165
Operating expenses:				
Selling and distribution	34,932	28,740	106,750	86,423
General and administrative	27,376	25,561	87,221	79,123
Other operating expense, net	1,733	1,103	5,731	861
Amortization expense	8,839	7,040	25,207	18,774
Total operating expenses	72,880	62,444	224,909	185,181
Operating income	52,652	47,793	130,989	119,984
Other expense (income):				
Interest expense, net	12,610	12,867	39,931	31,473
Gain on foreign currency exchange	(5,620)	(46)	(5,065)	(2,116)
Other expense (income), net	547	(1,838)	(170)	(3,044)
Total other expense	7,537	10,983	34,696	26,313
Income before income taxes	45,115	36,810	96,293	93,671
Income taxes	14,725	11,943	31,750	30,833
Net income	$ 30,390	$ 24,867	$ 64,543	$ 62,838
Weighted average common shares:				
Basic	35,967	35,421	35,721	34,870
Diluted	36,911	36,373	36,894	35,935
Net earnings per common share:				
Basic	$ .84	$ .70	$ 1.81	$ 1.80
Diluted	$ .82	$ .68	$ 1.75	$ 1.75

See Notes to Condensed Consolidated Financial Statements.

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TREEHOUSE FOODS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	Nine Months Ended September 30, 2011	Nine Months Ended September 30, 2010
	(Unaudited)	
Cash flows from operating activities:		
Net income	$ 64,543	$ 62,838
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	36,473	31,868
Amortization	25,207	18,774
(Gain) loss on foreign currency exchange	(274)	1,012
Mark to market adjustment on derivative contracts	(1,742)	(3,176)
Excess tax (benefits) deficiency from stock-based compensation	(3,888)	440
Stock-based compensation	12,573	11,817
Loss on disposition of assets, net	663	2,552
Write-down of tangible assets	2,891	
Deferred income taxes	5,303	7,918
Curtailment of postretirement benefit obligation		(2,357)
Other	121	121
Changes in operating assets and liabilities, net of acquisitions:		
Receivables	(23,806)	2,244
Inventories	(81,540)	459
Prepaid expenses and other assets	2,447	(4,592)
Accounts payable, accrued expenses and other liabilities	11,908	20,734
Net cash provided by operating activities	50,879	150,652
Cash flows from investing activities:		
Additions to property, plant and equipment	(52,817)	(30,477)
Additions to other intangible assets	(7,615)	(16,788)
Acquisition of business, net of cash acquired	3,243	(664,655)
Proceeds from sale of fixed assets	233	16
Net cash used in investing activities	(56,956)	(711,904)
Cash flows from financing activities:		
Proceeds from issuance of debt		400,000
Borrowings under revolving credit facility	225,600	324,600
Payments under revolving credit facility	(213,900)	(251,300)
Payments on capitalized lease obligations	(961)	(836)
Proceeds from issuance of common stock, net of expenses		110,688
Payment of deferred financing costs	(1,518)	(10,783)
Net payments related to stock-based award activities	(8,672)	(11,728)
Excess tax benefits (deficiency) from stock-based compensation	3,888	(440)
Net cash provided by financing activities	4,437	560,201
Effect of exchange rate changes on cash and cash equivalents	(1,603)	92
Net decrease in cash and cash equivalents	(3,243)	(959)
Cash and cash equivalents, beginning of period	6,323	4,415

Cash and cash equivalents, end of period	$	3,080	$	3,456

See Notes to Condensed Consolidated Financial Statements.

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TREEHOUSE FOODS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

As of and for the nine months ended September 30, 2011

(Unaudited)

1. Basis of Presentation

The unaudited Condensed Consolidated Financial Statements included herein have been prepared by TreeHouse Foods, Inc. (the Company, we, us, or our), pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) applicable to quarterly reporting on Form 10-Q. In our opinion, these statements include all adjustments necessary for a fair presentation of the results of all interim periods reported herein. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted as permitted by such rules and regulations. Certain product sales, as disclosed in Note 20, from prior year have been reclassified and certain line items on the Condensed Consolidated Statements of Cash Flows for the prior year have been combined to conform to the current period presentation. These reclassifications had no effect on reported net income, total assets, or cash flows. The Condensed Consolidated Financial Statements and related notes should be read in conjunction with the Consolidated Financial Statements and related notes included in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2010. Results of operations for interim periods are not necessarily indicative of annual results.

The preparation of our Condensed Consolidated Financial Statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires us to use our judgment to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent assets and liabilities at the date of the Condensed Consolidated Financial Statements, and the reported amounts of net sales and expenses during the reporting period. Actual results could differ from these estimates.

A detailed description of the Company s significant accounting policies can be found in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2010.

2. Recent Accounting Pronouncements

On September 21, 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2011-09, *Employer s Participation in Multiemployer Plans* which increases the quantitative and qualitative disclosures an employer is required to provide about its participation in significant multiemployer plans that offer pension and other postretirement benefits. This ASU does not change current accounting and thus the Company does not believe this ASU will have a significant impact on the Company s financial statements. This ASU is effective for fiscal years ended on or after December 15, 2011.

On September 15, 2011, the FASB issued ASU 2011-08, *Testing Goodwill for Impairment* which provides entities the option of performing a qualitative assessment of goodwill before calculating the fair value of a reporting unit in Step 1 of the goodwill impairment test. If an entity determines, based on the qualitative factors, that the fair value of a reporting unit is more likely than not less than the carrying amount, the two-step impairment test would be required. This ASU is effective for annual and interim periods for fiscal years beginning after December 15, 2011. Early adoption is permitted. This literature does not change how goodwill is accounted for, and thus the Company does not believe this ASU will have a significant impact on the Company s financial statements.

On June 16, 2011, the FASB issued ASU 2011-05, *Presentation of Comprehensive Income* which revises the manner in which entities present comprehensive income in their financial statements. This ASU removes the current presentation guidance and requires comprehensive income to be presented either in a single continuous statement of comprehensive income or two separate but consecutive statements. This guidance is effective for fiscal years and interim periods within those years, beginning after December 15, 2011. ASU 2011-05 does not change current accounting and therefore is not expected to have a significant impact on the Company s financial statements.

On May 12, 2011, the FASB issued ASU 2011-04, *Fair Value Measurement: Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs.* This ASU provides converged guidance on how (not when) to measure fair value. The ASU provides expanded disclosure requirements and other amendments, including those that eliminate unnecessary wording differences between U.S. GAAP and International Financial Reporting Standards (IFRSs). This ASU is effective for interim and annual periods beginning after December 15, 2011 and is not expected to have a significant impact on the Company s disclosures or fair value measurements.

3. Facility Closings

On February 28, 2011, the Company announced plans to close its pickle plant in Springfield, Missouri. Production ceased in August 2011 and has been transferred to other pickle facilities. Full plant closure is expected to occur by December 31, 2011. For the three and nine months ended September 30, 2011, the Company recorded costs of $1.4 million and $4.6 million, respectively. For the three months ended September 30, 2011, costs consisted of $0.4 million for severance and other costs, $0.1 million for fixed asset impairments and $0.9 million for disposal costs. For the nine months ended September 30, 2011, costs relating to this closure consisted of a fixed asset impairment charge of $2.4 million to reduce the carrying value of the facility to net realizable value, $0.6 million for severance and other costs, and $1.6 million for disposal costs. These costs are included in Other operating expense, net line in our Condensed Consolidated Statements of Income. Total costs are expected to be approximately $5.0 million. Components of the charges include $3.8 million for asset write-offs and removal of certain manufacturing equipment, $0.8 million in severance and other charges, and $0.4 million in costs to transfer inventory to other manufacturing facilities. The Company estimates that approximately $2.6 million of the charges will be in cash and incurred in 2011. The Company has accrued severance costs of approximately $0.3 million as of September 30, 2011 consisting of expense of $0.4 million less payments of $0.1 million.

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4. Acquisitions

On October 28, 2010, the Company acquired S.T. Specialty Foods, Inc (S.T. Foods), a wholly owned subsidiary of STSF Holdings, Inc. (Holdings) by acquiring all of the outstanding securities of Holdings for approximately $180 million in cash. The acquisition was funded by the Company s revolving credit facility. S.T. Foods, has annual net sales of approximately $100 million and is a manufacturer of private label macaroni and cheese, skillet dinners and other value-added side dishes. The acquisition added additional categories to our product portfolio for the retail grocery channel.

The Company s purchase price allocation as set forth in the Company s Annual Report of Form 10-K for the fiscal year ended December 31, 2010 was preliminary and subject to tax adjustments that were finalized during the third quarter of 2011.

On March 2, 2010, the Company acquired Sturm Foods, Inc. (Sturm), a private label manufacturer of hot cereals and powdered soft drink mixes that services retail and foodservice customers in the United States. The acquisition of Sturm has strengthened the Company s presence in private label dry grocery categories.

5. Inventories

	September 30, 2011	December 31, 2010
	(In thousands)	
Raw materials and supplies	$ 121,497	$ 111,376
Finished goods	264,276	194,558
LIFO reserve	(18,327)	(18,539)
Total	$ 367,446	$ 287,395

Approximately $101.6 million and $84.8 million of our inventory was accounted for under the LIFO method of accounting at September 30, 2011 and December 31, 2010, respectively.

6. Property, Plant and Equipment

	September 30, 2011	December 31, 2010
	(In thousands)	
Land	$ 18,626	$ 15,851
Buildings and improvements	150,185	148,616
Machinery and equipment	411,404	390,907
Construction in progress	43,143	21,067
Total	623,358	576,441
Less accumulated depreciation	(222,939)	(190,250)
Property, plant and equipment, net	$ 400,419	$ 386,191

7. Goodwill and Intangible Assets

Changes in the carrying amount of goodwill for the nine months ended September 30, 2011 are as follows:

	North American Retail Grocery		Food Away From Home		Industrial and Export		Total	
			(In thousands)					
Balance at December 31, 2010	$	850,593	$	92,146	$	133,582	$	1,076,321
Currency exchange adjustment		(3,357)		(230)				(3,587)
Purchase price adjustment		(2,869)		(9)				(2,878)
Balance at September 30, 2011	$	844,367	$	91,907	$	133,582	$	1,069,856

Purchase price adjustments are related to working capital, tax and other adjustments for the Sturm and S.T. Foods acquisitions. The Company has not incurred any goodwill impairments since its inception.

TREEHOUSE FOODS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The gross carrying amount and accumulated amortization of intangible assets other than goodwill as of September 30, 2011 and December 31, 2010 are as follows:

	September 30, 2011			December 31, 2010		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
	(In thousands)					
Intangible assets with indefinite lives:						
Trademarks	$ 31,827	$	$ 31,827	$ 32,673	$	$ 32,673
Intangible assets with finite lives:						
Customer-related	443,690	(75,675)	368,015	445,578	(57,480)	388,098
Non-compete agreement	1,000	(1,000)		1,000	(967)	33
Trademarks	20,010	(4,287)	15,723	20,010	(3,393)	16,617
Formulas/recipes	6,782	(2,953)	3,829	6,825	(1,972)	4,853
Computer software	33,253	(9,014)	24,239	26,007	(4,664)	21,343
Total	$ 536,562	$ (92,929)	$ 443,633	$ 532,093	$ (68,476)	$ 463,617

Amortization expense on intangible assets for the three months ended September 30, 2011 and 2010 was $8.8 million and $7.0 million, respectively, and $25.2 million and $18.8 million for the nine months ended September 30, 2011 and 2010, respectively. Estimated amortization expense on intangible assets for 2011 and the next four years is as follows:

	(In thousands)
2011	$ 33,768
2012	$ 32,081
2013	$ 30,744
2014	$ 30,503
2015	$ 29,563

8. Accounts Payable and Accrued Expenses

	September 30, 2011	December 31, 2010
	(In thousands)	
Accounts payable	$ 140,690	$ 112,638
Payroll and benefits	23,150	33,730
Interest and taxes	16,549	21,019
Health insurance, workers compensation and other insurance costs	5,938	4,855
Marketing expenses	6,121	10,165
Other accrued liabilities	9,530	19,977
Total	$ 201,978	$ 202,384

9. Income Taxes

Income tax expense was recorded at an effective rate of 32.6% and 33.0% for the three and nine months ended September 30, 2011, respectively, compared to 32.4% and 32.9% for the three and nine months ended September 30, 2010, respectively. The Company s effective tax rate is favorably impacted by an intercompany financing structure with its Canadian subsidiary E.D. Smith.

As of September 30, 2011, the Company does not believe that its gross recorded unrecognized tax benefits will materially change within the next 12 months.

The Company or one of its subsidiaries files income tax returns in the U.S., Canada and various state jurisdictions. The Company has various state tax examinations in process, which are expected to be completed in 2011 or 2012. The outcome of the various state tax examinations is unknown at this time.

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TREEHOUSE FOODS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

10. Long-Term Debt

	September 30, 2011	December 31, 2010
	(In thousands)	
Revolving credit facility	$ 484,300	$ 472,600
High yield notes	400,000	400,000
Senior notes	100,000	100,000
Tax increment financing and other debt	8,415	4,828
Total debt outstanding	992,715	977,428
Less current portion	(2,241)	(976)
Total long-term debt	$ 990,474	$ 976,452

Revolving Credit Facility On September 23, 2011, the Company entered into Amendment No.1 (Amendment) to the Amended and Restated Credit Agreement (Credit Agreement) with Bank of America, N.A., as administrative agent, and the group of other participating lenders. The amendment, among other things, extends the maturity of the revolving credit facility to September 23, 2016, and adjusts the interest rates. The interest rates under the Credit Agreement are based on the Company s consolidated leverage ratio, and are determined by either LIBOR plus a margin ranging from 1.00% to 1.60% or a base rate (as defined in the Credit Agreement) plus a margin ranging from 0.00% to 0.60%. In addition, a facility fee ranging from 0.25% to 0.40% is due quarterly on the aggregate commitment under the revolving credit facility. The Company s unsecured revolving credit facility has an aggregate commitment of $750 million, of which $256.5 million was available as of September 30, 2011. As of September 30, 2011, there were $9.2 million in letters of credit under the revolving credit facility that were issued but undrawn. The revolving credit facility contains various financial and other restrictive covenants and requires that the Company maintains certain financial ratios, including a leverage and interest coverage ratio. The Company is in compliance with all applicable covenants as of September 30, 2011. The Company s average interest rate on debt outstanding under the revolving credit facility for the three and nine months ended September 30, 2011 was 2.09% and 2.14%, respectively.

High Yield Notes The Company s 7.75% high yield notes in aggregate principal amount of $400 million are due March 1, 2018 (the Notes). The Notes are guaranteed by the Company s wholly owned subsidiaries Bay Valley Foods, LLC; EDS Holdings, LLC; Sturm Foods, Inc.; STSF Holdings, Inc. and S.T. Specialty Foods, Inc. and certain other of our subsidiaries that may become guarantors from time to time in accordance with the applicable Indenture and may fully, jointly, severally and unconditionally guarantee our payment obligations under any series of debt securities offered. The Indenture governing the Notes provides, among other things, that the Notes will be senior unsecured obligations of the Company. The Indenture contains various restrictive covenants of which the Company is in compliance as of September 30, 2011.

Senior Notes The Company has outstanding $100 million in aggregate principal of 6.03% senior notes due September 30, 2013, issued in a private placement pursuant to a Note Purchase Agreement among the Company and a group of purchasers. The Note Purchase Agreement contains covenants that will limit the ability of the Company and its subsidiaries to, among other things, merge with other entities, change the nature of the business, create liens, incur additional indebtedness or sell assets. The Note Purchase Agreement also requires the Company to maintain certain financial ratios. The Company is in compliance with the applicable covenants as of September 30, 2011.

Tax Increment Financing The Company owes $2.3 million related to redevelopment bonds pursuant to a Tax Increment Financing Plan and has agreed to make certain payments with respect to the principal amount of the bonds through May 2019.

11. Earnings Per Share

Basic earnings per share is computed by dividing net income by the number of weighted average common shares outstanding during the reporting period. The weighted average number of common shares used in the diluted earnings per share calculation is determined using the treasury stock method and includes the incremental effect related to outstanding stock options, restricted stock, restricted stock units and performance units.

TREEHOUSE FOODS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table summarizes the effect of the share-based compensation awards on the weighted average number of shares outstanding used in calculating diluted earnings per share:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
	(In thousands)		(In thousands)	
Weighted average common shares outstanding	35,967	35,421	35,721	34,870
Assumed exercise/vesting of equity awards (1)	944	952	1,173	1,065
Weighted average diluted common shares outstanding	36,911	36,373	36,894	35,935

(1) Incremental shares from stock options, restricted stock, restricted stock units, and performance units are computed by the treasury stock method. Stock options, restricted stock, restricted stock units, and performance units excluded from our computation of diluted earnings per share because they were anti-dilutive, were 110.2 thousand and 240.7 thousand for the three and nine months ended September 30, 2011, respectively, and 132.9 thousand and 132.8 thousand for the three and nine months ended September 30, 2010, respectively.

12. Stock-Based Compensation

Income before income taxes for the three and nine month periods ended September 30, 2011 and 2010 includes share-based compensation expense of \$3.1 million, \$12.6 million, \$4.0 million and \$11.8 million, respectively. The tax benefit recognized related to the compensation cost of these share-based awards was approximately \$1.2 million, \$4.9 million, \$1.5 million and \$4.6 million for the three and nine month periods ended September 30, 2011 and 2010, respectively.

The following table summarizes stock option activity during the nine months ended September 30, 2011. Stock options are granted under our long-term incentive plan, and have a three year vesting schedule, which vest one-third on each of the first three anniversaries of the grant date. Stock options expire ten years from the grant date.

	Employee Options	Director Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (yrs)	Aggregate Intrinsic Value
	(In thousands)				(In thousands)
Outstanding, December 31, 2010	2,257	95	$ 28.38	5.6	$ 53,401
Granted	110		$ 54.90		
Forfeited			$		
Exercised	(108)		$ 25.86		
Outstanding, September 30, 2011	2,259	95	$ 29.74	5.1	$ 75,567