

MCCORMICK & CO INC
Form 10-Q
July 01, 2015
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q
QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For Quarter Ended May 31, 2015
Commission File Number 001-14920

McCORMICK & COMPANY, INCORPORATED
(Exact name of registrant as specified in its charter)

MARYLAND 52-0408290
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

18 Loveton Circle, P. O. Box 6000, 21152-6000
Sparks, MD (Address of principal executive offices) (Zip Code)
Registrant's telephone number, including area code (410) 771-7301

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 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 (Section 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 definition of "accelerated filer," "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer Accelerated Filer
Non-Accelerated Filer 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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

	Shares Outstanding
Common Stock	May 31, 2015 11,896,423
Common Stock Non-Voting	115,964,859

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

McCORMICK & COMPANY, INCORPORATED
 CONDENSED CONSOLIDATED INCOME STATEMENT (UNAUDITED)
 (in millions except per share amounts)

	Three months ended May 31,		Six months ended May 31,	
	2015	2014	2015	2014
Net sales	\$1,024.1	\$1,033.4	\$2,034.5	\$2,026.8
Cost of goods sold	620.1	620.9	1,240.8	1,222.8
Gross profit	404.0	412.5	793.7	804.0
Selling, general and administrative expense	281.2	290.8	548.8	557.7
Special charges	19.0	—	47.4	—
Operating income	103.8	121.7	197.5	246.3
Interest expense	13.0	12.5	25.9	24.9
Other income, net	0.6	0.3	0.4	0.5
Income from consolidated operations before income taxes	91.4	109.5	172.0	221.9
Income taxes	14.5	31.2	34.5	66.2
Net income from consolidated operations	76.9	78.3	137.5	155.7
Income from unconsolidated operations	7.4	6.2	17.3	11.3
Net income	\$84.3	\$84.5	\$154.8	\$167.0
Earnings per share – basic	\$0.66	\$0.65	\$1.21	\$1.28
Average shares outstanding – basic	127.9	130.2	128.1	130.6
Earnings per share – diluted	\$0.65	\$0.64	\$1.20	\$1.27
Average shares outstanding – diluted	129.0	131.2	129.2	131.7
Cash dividends paid per share	\$0.40	\$0.37	\$0.80	\$0.74

See notes to condensed consolidated financial statements (unaudited).

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McCORMICK & COMPANY, INCORPORATED
 CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (UNAUDITED)
 (in millions)

	Three months ended May 31,		Six months ended May 31,	
	2015	2014	2015	2014
Net income	\$84.3	\$84.5	\$154.8	\$167.0
Net income attributable to non-controlling interest	1.2	0.7	2.4	1.7
Other comprehensive income (loss):				
Unrealized components of pension plans	6.2	4.1	15.8	7.9
Currency translation adjustments	(13.4) (0.2) (150.6) 4.1
Change in derivative financial instruments	(0.7) (0.3) 0.5	—
Deferred taxes	(1.9) (1.4) (4.4) (2.9
Comprehensive income	\$75.7	\$87.4	\$18.5	\$177.8

See notes to condensed consolidated financial statements (unaudited).

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MCCORMICK & COMPANY, INCORPORATED
 CONDENSED CONSOLIDATED BALANCE SHEET
 (in millions)

	May 31, 2015 (unaudited)	May 31, 2014 (unaudited)	November 30, 2014
ASSETS			
Current Assets			
Cash and cash equivalents	\$89.5	\$81.4	\$77.3
Trade accounts receivables, net	390.6	417.1	493.6
Inventories			
Finished products	323.8	313.4	303.2
Raw materials and work-in-process	414.7	373.9	410.6
	738.5	687.3	713.8
Prepaid expenses and other current assets	140.3	138.9	131.5
Total current assets	1,358.9	1,324.7	1,416.2
Property, plant and equipment	1,486.2	1,448.0	1,481.4
Less: accumulated depreciation	(896.1)	(873.0)	(878.7)
Property, plant and equipment, net	590.1	575.0	602.7
Goodwill	1,719.8	1,798.6	1,722.2
Intangible assets, net	364.6	340.4	330.8
Investments and other assets	345.0	370.6	342.4
Total assets	\$4,378.4	\$4,409.3	\$4,414.3
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current Liabilities			
Short-term borrowings	\$416.7	\$307.1	\$269.6
Current portion of long-term debt	205.9	1.3	1.2
Trade accounts payable	337.8	335.8	372.1
Other accrued liabilities	378.4	358.6	479.1
Total current liabilities	1,338.8	1,002.8	1,122.0
Long-term debt	807.9	1,016.8	1,014.1
Other long-term liabilities	496.4	409.8	468.8
Total liabilities	2,643.1	2,429.4	2,604.9
Shareholders' Equity			
Common stock	378.0	363.5	367.2
Common stock non-voting	641.6	620.6	628.4
Retained earnings	1,020.4	969.3	982.6
Accumulated other comprehensive income (loss)	(324.7)	8.8	(186.0)
Non-controlling interests	20.0	17.7	17.2
Total shareholders' equity	1,735.3	1,979.9	1,809.4
Total liabilities and shareholders' equity	\$4,378.4	\$4,409.3	\$4,414.3
See notes to condensed consolidated financial statements (unaudited).			

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McCORMICK & COMPANY, INCORPORATED
 CONDENSED CONSOLIDATED CASH FLOW STATEMENT (UNAUDITED)
 (in millions)

	Six months ended May 31,	
	2015	2014
Operating activities		
Net income	\$154.8	\$167.0
Adjustments to reconcile net income to net cash flow provided by operating activities:		
Depreciation and amortization	52.5	53.5
Stock-based compensation	13.9	12.1
Income from unconsolidated operations	(17.3)	(11.3)
Changes in operating assets and liabilities	(35.2)	(51.6)
Dividends from unconsolidated affiliates	17.2	12.4
Net cash flow provided by operating activities	185.9	182.1
Investing activities		
Acquisition of businesses (net of cash acquired)	(111.5)	—
Capital expenditures	(42.7)	(47.4)
Proceeds from sale of property, plant and equipment	0.1	0.7
Net cash flow used in investing activities	(154.1)	(46.7)
Financing activities		
Short-term borrowings, net	148.2	94.3
Long-term debt repayments	(0.3)	(1.2)
Proceeds from exercised stock options	14.2	16.1
Common stock acquired by purchase	(69.9)	(126.3)
Dividends paid	(102.5)	(96.7)
Net cash flow used in financing activities	(10.3)	(113.8)
Effect of exchange rate changes on cash and cash equivalents	(9.3)	(3.2)
Increase in cash and cash equivalents	12.2	18.4
Cash and cash equivalents at beginning of period	77.3	63.0
Cash and cash equivalents at end of period	\$89.5	\$81.4
See notes to condensed consolidated financial statements (unaudited).		

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McCORMICK & COMPANY, INCORPORATED
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. ACCOUNTING POLICIES

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and do not include all the information and notes required by United States generally accepted accounting principles (U.S. GAAP) for complete financial statements. In our opinion, the accompanying condensed consolidated financial statements contain all adjustments, which are of a normal and recurring nature, necessary to present fairly the financial position and the results of operations for the interim periods presented. The results of consolidated operations for the three and six month periods ended May 31, 2015 are not necessarily indicative of the results to be expected for the full year. Historically, our net sales, net income and cash flow from operations are lower in the first half of the fiscal year and increase in the second half. The typical increase in net sales, net income and cash flow from operations in the second half of the year is largely due to the consumer business cycle in the U.S., where customers typically purchase more products in the fourth quarter due to the Thanksgiving and Christmas holiday seasons.

For further information, refer to the consolidated financial statements and notes included in our Annual Report on Form 10-K for the year ended November 30, 2014.

Accounting and Disclosure Changes

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2014-09 Revenue from Contracts with Customers (Topic 606). This guidance is intended to improve and converge with international standards the financial reporting requirements for revenue from contracts with customers. It will be effective for our first quarter of 2018, unless amended to a later date, and early adoption is not permitted. We have not yet determined the impact from adoption of this new accounting pronouncement on our financial statements.

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2. ACQUISITIONS

Acquisitions are part of our strategy to increase sales and profits.

On March 9, 2015, we acquired 100% of the shares of Brand Aromatics, a privately held company located in the U.S. Brand Aromatics is a supplier of natural savory flavors, marinades, and broth and stock concentrates to the packaged food industry. Its addition expands the breadth of value-added products in our industrial business. The purchase price for Brand Aromatics was \$62.5 million, subject to certain closing adjustments, and was financed with a combination of cash and short-term borrowings. At the time of acquisition, annual sales of Brand Aromatics were approximately \$30 million. As of May 31, 2015, a preliminary valuation of the acquired net assets of Brand Aromatics resulted in \$5.1 million allocated to tangible net assets, \$19.5 million allocated to other intangible assets and \$37.9 million allocated to goodwill. Goodwill related to the Brand Aromatics acquisition, which will be deductible for tax purposes, primarily represents the intangible assets that do not qualify for separate recognition, such as expected synergies from the extension of our customer intimacy and value-added flavor solutions we provide to our industrial customers to stocks, marinades and other savory flavors, as well as from the combined operations and assembled workforces, and the future development initiatives of the assembled workforces. The preliminary valuation, based on a comparison of acquisitions of similar industrial businesses, provided average percentages of purchase prices assigned to goodwill and other identifiable intangible assets, which we used to initially value the Brand Aromatics acquisition. We expect to finalize the determination of the fair value of the acquired net assets of Brand Aromatics during the second half of 2015. Included in our industrial business segment since its acquisition, Brand Aromatics added \$4.8 million to sales in the second quarter 2015; its operating income contribution was not significant to our overall results.

On May 29, 2015, we completed the purchase of 100% of the shares of Drogheria & Alimentari (D&A), a privately held company based in Italy, and a leader of the spice and seasoning category in Italy that supplies both branded and private label products to consumers. The purchase price for D&A consisted of a cash payment of \$49.0 million, net of cash acquired of \$2.8 million, at the time of acquisition, subject to certain closing adjustments, and was financed with a combination of cash and short-term borrowings. In addition, the purchase agreement calls for a potential earn out payment in 2018 of up to €35 million, based upon the performance of the acquired business in 2017. This potential earn out payment has a preliminary acquisition-date fair value of \$26.0 million as of May 31, 2015 (or approximately €24 million), based on recent estimates of projected performance in 2017 furnished by the sellers, which we used to estimate the contingent consideration payable in 2018 and discounted using a probability-weighted approach. At the time of the acquisition, annual sales of D&A were approximately €50 million. As of May 31, 2015, a preliminary valuation of the acquired net assets of D&A resulted in \$7.2 million allocated to tangible net assets, \$24.3 million allocated to other intangible assets and \$43.5 million allocated to goodwill. Goodwill related to the D&A acquisition, which is not deductible for tax purposes, primarily represents the intangible assets that do not qualify for separate recognition, such as the value of leveraging our brand building expertise, our customer insights in demand from consumers for unique and authentic ethnic flavors and our supply chain capabilities, as well as expected synergies from the combined operations and assembled workforce. The preliminary valuation, based on a comparison of acquisitions of similar consumer businesses, provided average percentages of purchase prices assigned to goodwill and other intangible assets which we used to initially value the D&A acquisition. We expect to finalize the determination of the fair value of the acquired net assets of D&A, as well as the acquisition-date fair value of the contingent consideration, during the second half of 2015. D&A is included in our consumer business segment since its acquisition but, due to the timing of the acquisition, had no impact on our results of operations in the second quarter of 2015.

During the three and six months ended May 31, 2015, we recorded \$0.9 million and \$2.0 million, respectively, in transaction-related expenses associated with these acquisitions.

3. SPECIAL CHARGES

We continue to evaluate changes to our organization structure to enable us to reduce fixed costs, simplify or improve processes, and improve our competitiveness.

In late 2013, we announced a reorganization in parts of the Europe, Middle East and Africa (EMEA) region to further improve EMEA's profitability and process standardization while supporting its competitiveness and long-term growth. These actions included the closure of our current sales and distribution operations in The Netherlands, with the transition to a third-party distributor model to continue to sell the Silvo brand, as well as actions intended to reduce selling, general and administrative

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activities throughout EMEA, including the centralization of shared service activity across the region into Poland. In fiscal years 2013 and 2014, we recorded a total of \$27.1 million of cash and non-cash charges related to this reorganization. We expect to realize annual cost savings of approximately \$10 million in 2015 related to this EMEA reorganization.

The following table outlines the major components of accrual balances and activity relating to the special charges associated with the EMEA reorganization plan undertaken in 2013 and 2014 for the six months ended May 31, 2015 (in millions):

Employee severance and related benefits	Other related costs
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