

TREX CO INC
Form 10-Q
May 08, 2015
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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, 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: 001-14649

Trex Company, Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)
160 Exeter Drive
Winchester, Virginia
(Address of principal executive offices)
Registrant's telephone number, including area code: (540) 542-6300

54-1910453
(I.R.S. Employer
Identification No.)
22603-8605
(Zip Code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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 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.:

Large accelerated filer Accelerated filer

Non-accelerated filer Smaller reporting company

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

The number of shares of the registrant's common stock, par value \$.01 per share, outstanding at April 21, 2015 was 32,079,980 shares.

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PART I
FINANCIAL INFORMATION

Item 1. Financial Statements**TREX COMPANY, INC.****Condensed Consolidated Balance Sheets**

(In thousands)

	March 31, 2015 (Unaudited)	December 31, 2014
Assets		
Current assets:		
Cash and cash equivalents	\$ 2,556	\$ 9,544
Accounts receivable, net	136,993	36,391
Inventories	22,920	23,747
Prepaid expenses and other current assets	2,137	6,288
Deferred income taxes	9,271	9,271
Total current assets	173,877	85,241
Property, plant and equipment, net	104,163	98,716
Goodwill and other intangibles	10,532	10,534
Other assets	1,311	1,333
Total assets	\$ 289,883	\$ 195,824
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	\$ 12,785	\$ 20,050
Accrued expenses	20,951	20,660
Accrued warranty	8,738	8,744
Line of credit	84,000	
Total current liabilities	126,474	49,454
Deferred income taxes	3,708	3,708
Non-current accrued warranty	24,045	25,097
Other long-term liabilities	4,117	4,180
Total liabilities	158,344	82,439

Stockholders' equity:

Preferred stock, \$0.01 par value, 3,000,000 shares authorized; none issued and outstanding		
Common stock, \$0.01 par value, 80,000,000 shares authorized; 34,860,283 and 34,800,552 shares issued and 32,079,854 and 32,020,123 shares outstanding at March 31, 2015 and December 31, 2014, respectively	349	348
Additional paid-in capital	117,340	116,740
Retained earnings	88,850	71,297
Treasury stock, at cost, 2,780,429 shares at March 31, 2015 and December 31, 2014	(75,000)	(75,000)
Total stockholders' equity	131,539	113,385
Total liabilities and stockholders' equity	\$ 289,883	\$ 195,824

See Accompanying Notes to Condensed Consolidated

Financial Statements (Unaudited).

Table of Contents**TREX COMPANY, INC.****Condensed Consolidated Statements of Comprehensive Income**

(Unaudited)

(In thousands, except share and per share data)

	Three Months Ended March 31,	
	2015	2014
Net sales	\$ 120,800	\$ 100,645
Cost of sales	72,553	62,478
Gross profit	48,247	38,167
Selling, general and administrative expenses	20,593	18,222
Income from operations	27,654	19,945
Interest expense, net	137	323
Income before income taxes	27,517	19,622
Provision for income taxes	9,964	7,327
Net income	\$ 17,553	\$ 12,295
Basic earnings per common share	\$ 0.55	\$ 0.37
Basic weighted average common shares outstanding	31,683,672	33,128,676
Diluted earnings per common share	\$ 0.55	\$ 0.37
Diluted weighted average common shares outstanding	32,094,828	33,599,438
Comprehensive income	\$ 17,553	\$ 12,295

See Accompanying Notes to Condensed Consolidated

Financial Statements (Unaudited).

Table of Contents**TREX COMPANY, INC.****Condensed Consolidated Statements of Cash Flows**

(Unaudited)

(In thousands)

	Three Months Ended	
	March 31,	
	2015	2014
Operating Activities		
Net income	\$ 17,553	\$ 12,295
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	3,636	3,797
Deferred income taxes		352
Stock-based compensation	1,454	1,170
Gain on disposal of property, plant and equipment		(37)
Excess tax benefits from stock compensation	(1,035)	(6,507)
Changes in operating assets and liabilities:		
Accounts receivable	(100,602)	(79,152)
Inventories	827	(7,785)
Prepaid expenses and other assets	888	(82)
Accounts payable	(7,265)	(3,892)
Accrued expenses and other liabilities	(5,666)	(9,068)
Income taxes receivable/payable	9,166	6,884
Net cash used in operating activities	(81,044)	(82,025)
Investing Activities		
Expenditures for property, plant and equipment	(9,060)	(3,188)
Proceeds from sales of property, plant and equipment		37
Purchase of acquired company, net of cash acquired	(31)	(44)
Notes receivable, net		19
Net cash used in investing activities	(9,091)	(3,176)
Financing Activities		
Borrowings under line of credit	84,000	85,000
Principal payments under line of credit		(5,000)
Repurchases of common stock	(2,015)	(1,433)
Proceeds from employee stock purchase and option plans	127	84
Excess tax benefits from stock compensation	1,035	6,507
Net cash provided by financing activities	83,147	85,158

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Net decrease in cash and cash equivalents	(6,988)	(43)
Cash and cash equivalents at beginning of period	9,544	3,772
Cash and cash equivalents at end of period	\$ 2,556	\$ 3,729
Supplemental Disclosure:		
Cash paid for interest, net of capitalized interest	\$ 59	\$ 99
Cash paid for income taxes, net	\$ 799	\$ 91

See Accompanying Notes to Condensed Consolidated

Financial Statements (Unaudited).

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TREX COMPANY, INC.

Notes to Condensed Consolidated Financial Statements

For the Three Months Ended March 31, 2015 and 2014

(Unaudited)

1. BUSINESS AND ORGANIZATION

Trex Company, Inc. (the Company) is the world's largest manufacturer of wood-alternative decking and railing products, which are marketed under the brand name Trex®. The Company is incorporated in Delaware. The principal executive offices are located at 160 Exeter Drive, Winchester, Virginia 22603, and the telephone number at that address is (540) 542-6300. The Company operates in one business segment.

2. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, the accompanying condensed consolidated financial statements do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments (consisting of normal and recurring adjustments except as otherwise described herein) considered necessary for a fair presentation have been included in the accompanying condensed consolidated financial statements. All common stock share and per share data for all historical periods presented have been retroactively adjusted to reflect a two-for-one stock split distributed on May 7, 2014. The consolidated results of operations for the three months ended March 31, 2015 are not necessarily indicative of the results that may be expected for the full fiscal year. These condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements as of December 31, 2014 and 2013 and for each of the three years in the period ended December 31, 2014 included in the annual report of Trex Company, Inc. on Form 10-K, as filed with the Securities and Exchange Commission.

The Company's critical accounting policies are included in the Company's Annual Report on Form 10-K for the year ended December 31, 2014.

3. NEW ACCOUNTING STANDARDS

In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update 2014-09, *Revenue from Contracts with Customers*. The new standard provides a single, comprehensive model for revenue arising from contracts with customers and supersedes most current revenue recognition guidance. The new standard requires an entity to recognize revenue at an amount that reflects the consideration to which the company expects to be entitled in exchange for transferring goods or services to a customer. The new guidance is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016 and allows for either full retrospective or modified retrospective application. No early adoption is permitted. The Company is currently assessing the impact of the adoption of this new standard on its consolidated financial statements and footnote disclosures and has not yet selected a method of adoption.

4. INVENTORIES

Inventories, at LIFO (last-in, first-out) value, consist of the following (in thousands):

	March 31, 2015	December 31, 2014
Finished goods	\$ 32,537	\$ 32,756
Raw materials	15,682	16,290
Total FIFO inventories	48,219	49,046
Reserve to adjust inventories to LIFO value	(25,299)	(25,299)
Total LIFO inventories	\$ 22,920	\$ 23,747

The Company utilizes the last-in, first-out (LIFO) method of accounting for inventory, which generally provides matching of current costs with current revenues. However, under the LIFO method, reductions in annual inventory balances cause a portion of the Company's cost of sales to be based on historical costs rather than current year costs (LIFO liquidation). Reductions in interim inventory balances expected to be replenished by year-end do not result in a LIFO liquidation. Accordingly, interim LIFO calculations are based, in part, on management's estimates of expected year-end inventory levels and costs which may differ from actual results. There were no LIFO inventory liquidations or related impact on cost of sales in the three months ended March 31, 2015 or 2014.

Table of Contents**5. ACCRUED EXPENSES**

Accrued expenses consist of the following (in thousands):

	March 31, 2015	December 31, 2014
Accrued compensation and benefits	\$ 6,027	\$ 9,201
Income taxes payable	4,868	
Accrued sales and marketing	4,618	5,963
Accrued rent obligations	1,377	1,372
Accrued manufacturing expenses	1,215	1,307
Other	2,846	2,817
Total accrued expenses	\$ 20,951	\$ 20,660

6. DEBT

The Company's outstanding debt consists of a revolving credit facility.

Revolving Credit Facility

The Company currently has a Second Amended Credit Agreement that provides the Company with one or more revolving loans in a collective maximum principal amount of \$150 million from January 1 through June 30 of each year, reducing to a maximum principal amount of \$100 million from July 1 through December 31 of each year throughout the term, which ends November 20, 2019.

At March 31, 2015, the Company had \$84 million of outstanding borrowings under its revolving credit facility and remaining available borrowing capacity of approximately \$66 million.

Compliance with Debt Covenants and Restrictions

The Company's ability to make scheduled principal and interest payments and to borrow and repay amounts under any outstanding revolving credit facility, and continue to comply with any loan covenants depends primarily on the Company's ability to generate sufficient cash flow from operations.

As of March 31, 2015, the Company was in compliance with all of the covenants contained in its debt agreements. Failure to comply with the loan covenants might cause lenders to accelerate the repayment obligations under the credit facility, which may be declared payable immediately based on a default.

7. FINANCIAL INSTRUMENTS

The Company considers the recorded value of its financial assets and liabilities, consisting primarily of cash and cash equivalents, accounts receivable, accounts payable, accrued expenses and other current liabilities to approximate the fair value of the respective assets and liabilities at March 31, 2015 and December 31, 2014.

8. STOCKHOLDERS EQUITY*Earnings Per Share*

The following table sets forth the computation of basic and diluted earnings per share (in thousands, except share and per share data):

	Three Months Ended March 31,	
	2015	2014
Numerator:		
Net income available to common shareholders	\$ 17,553	\$ 12,295
Denominator:		
Basic weighted average shares outstanding	31,683,672	33,128,676
Effect of dilutive securities:		
SARs and options	240,066	302,914

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	Three Months Ended March 31,	
	2015	2014
Restricted stock	171,090	167,848
Diluted weighted average shares outstanding	32,094,828	33,599,438
Basic earnings per share	\$ 0.55	\$ 0.37
Diluted earnings per share	\$ 0.55	\$ 0.37

Diluted earnings per share is computed using the weighted average number of shares determined for the basic earnings per share computation plus the dilutive effect of common stock equivalents using the treasury stock method. The computation of diluted earnings per share excludes the following potentially dilutive securities because the effect would be anti-dilutive:

	Three Months Ended March 31,	
	2015	2014
Restricted stock and stock options		88
Stock appreciation rights		1,196

Stock Repurchase Programs

On October 23, 2014, the Company's Board of Directors authorized a common stock repurchase program of up to two million shares of the Company's outstanding common stock (the October 2014 Stock Repurchase Program). This authorization has no expiration date. As of March 31, 2015, the Company made no repurchases under the October 2014 Stock Repurchase Program.

9. STOCK-BASED COMPENSATION

The Company has one stock-based compensation plan, the 2014 Stock Incentive Plan (the Plan), approved by the Company's stockholders in April 2014. The Plan amended and restated in its entirety the Trex Company, Inc. 2005 Stock Incentive Plan. The Plan is administered by the Compensation Committee of the Company's Board of Directors. Stock-based compensation is granted to officers, directors and certain key employees in accordance with the provisions of the Plan. The Plan provides for grants of stock options, restricted stock, restricted stock units, stock appreciation rights (SARs), and unrestricted stock. As of March 31, 2015, the total aggregate number of shares of the Company's common stock that may be issued under the Plan is 6,420,000.

In 2014, the Company began granting performance-based restricted stock in addition to the time-based restricted stock it previously granted. The performance-based restricted shares have a three-year vesting period, vesting one-third each year based on target earnings before interest, taxes, depreciation and amortization, or EBITDA, for 1 year, cumulative 2 years and cumulative 3 years, respectively. With respect to each vesting, the number of shares that will vest will be between 0% and 200% of the target number of shares.

The fair value of each SAR is estimated on the date of grant using a Black-Scholes option-pricing formula. For SARs issued in the three months ended March 31, 2015 and 2014, respectively, the assumptions shown in the following table were used:

	Three Months Ended March 31,	
	2015	2014
Weighted-average fair value of grants	\$ 17.10	\$ 18.70
Dividend yield	0%	0%
Average risk-free interest rate	1.7%	1.8%
Expected term (years)	5	5
Expected volatility	44%	54%

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The following table summarizes the Company's stock-based compensation grants for the three months ended March 31, 2015:

	Stock Awards Granted	Weighted-Average Grant Price Per Share
Time-based restricted stock	43,738	\$ 43.89
Performance-based restricted stock	34,638	\$ 43.89
Stock appreciation rights	201	\$ 42.47

The Company recognizes stock-based compensation expense ratably over the period from the grant date to the earlier of: (1) the vesting date of the award, or (2) the date the grantee is eligible to retire without forfeiting the award. For performance-based restricted stock, expense is recognized ratably over the performance and vesting period of each tranche based on management's judgment of the ultimate award that is likely to be paid out based on the achievement of the predetermined performance measures. The following table summarizes the Company's stock-based compensation expense for the three months ended March 31, 2015 and 2014 (in thousands):