

GENESEE & WYOMING INC
Form 10-Q
May 07, 2018
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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 March 31, 2018

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 001-31456

GENESEE & WYOMING INC.

(Exact name of registrant as specified in its charter)

Delaware 06-0984624
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)
20 West Avenue, Darien, Connecticut 06820
(Address of principal executive offices)(Zip
Code)
(203) 202-8900
(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, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the

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Exchange Act.

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

Shares of common stock outstanding as of the close of business on May 1, 2018:

Class	Number of Shares Outstanding
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Class A Common Stock	60,149,625
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Class B Common Stock	671,138
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Unless the context otherwise requires, when used in this Quarterly Report on Form 10-Q, the terms "Genesee & Wyoming," "G&W," the "Company," "we," "our" and "us" refer to Genesee & Wyoming Inc. and its subsidiaries. All references to currency amounts included in this Quarterly Report on Form 10-Q, including the financial statements, are in United States dollars unless specifically noted otherwise. The term carload represents physical railcars and the estimated railcar equivalents of commodities transported by metric ton or other measure, as well as intermodal units. From time to time, we may use our website as a channel of distribution of material company information. Financial and other material information regarding the Company is routinely posted on and accessible at www.gwrr.com/investors. In addition, you may automatically receive email alerts and other information about us by enrolling your email address in the "Email Alerts" section of www.gwrr.com/investors. The information contained on or connected to our Internet website is not deemed to be incorporated by reference in this Quarterly Report or filed with the Securities and Exchange Commission.

Forward-Looking Statements

This report and other documents referred to in this report contain forward-looking statements regarding future events and the future performance of Genesee & Wyoming Inc. that are based on current expectations, estimates and projections about our industry, our business and our performance, management's beliefs and assumptions made by management. Words such as "anticipates," "intends," "plans," "believes," "could," "should," "seeks," "expects," "will," "estimates," "trends," "outlook," variations of these words and similar expressions are intended to identify these forward-looking statements. These statements are not guarantees of future performance and are subject to certain risks, uncertainties and assumptions that are difficult to forecast, including the following: risks related to the operation of our railroads; severe weather conditions and other natural occurrences, which could result in shutdowns, derailments, railroad network and port congestion or other substantial disruption of operations; customer demand and changes in our operations or loss of important customers; exposure to the credit risk of customers and counterparties; changes in commodity prices; consummation and integration of acquisitions; implementation of restructuring plans; economic, political and industry conditions, including employee strikes or work stoppages; retention and contract continuation; legislative and regulatory developments, including changes in environmental and other laws and regulations to which we or our customers are subject; increased competition in relevant markets; funding needs and financing sources, including our ability to obtain government funding for capital projects; international complexities of operations, currency fluctuations, finance, tax and decentralized management; challenges of managing rapid growth, including retention and development of senior leadership; unpredictability of fuel costs; susceptibility to and outcome of various legal claims, lawsuits and arbitrations; increase in, or volatility associated with, expenses related to estimated claims, self-insured retention amounts and insurance coverage limits; consummation of new business opportunities; decrease in revenues and/or increase in costs and expenses; susceptibility to the risks of doing business in foreign countries; uncertainties arising from a referendum in which voters in the United Kingdom (U.K.) approved an exit from the European Union (E.U.), commonly referred to as Brexit; our ability to integrate acquired businesses successfully or to realize the expected synergies associated with acquisitions; risks associated with our substantial indebtedness; failure to maintain satisfactory working relationships with partners in Australia; failure to maintain an effective system of internal control over financial reporting as well as disclosure controls and procedures and others including, but not limited to, those set forth in Part II Item 1A of this Quarterly Report on Form 10-Q, if any, and those noted in our 2017 Annual Report on Form 10-K under "Risk Factors." Therefore, actual results may differ materially from those expressed or forecasted in any such forward-looking statements. Forward-looking statements speak only as of the date of this report or as of the date they were made. We do not undertake, and expressly disclaim, any duty to publicly update any forward-looking statement, whether as a result of new information, future events, or otherwise, except as required by law.

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

GENESEE & WYOMING INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

AS OF MARCH 31, 2018 and DECEMBER 31, 2017 (Unaudited)

(dollars in thousands, except per share and share amounts)

	March 31, 2018	December 31, 2017
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$121,390	\$80,472
Accounts receivable, net	422,727	416,705
Materials and supplies	56,035	57,750
Prepaid expenses and other	52,968	34,606
Total current assets	653,120	589,533
PROPERTY AND EQUIPMENT, net	4,640,824	4,656,921
GOODWILL	1,162,657	1,165,587
INTANGIBLE ASSETS, net	1,562,007	1,567,038
DEFERRED INCOME TAX ASSETS, net	3,465	3,343
OTHER ASSETS	48,703	52,475
Total assets	\$8,070,776	\$8,034,897
LIABILITIES AND EQUITY		
CURRENT LIABILITIES:		
Current portion of long-term debt	\$50,952	\$27,853
Accounts payable	251,875	253,993
Accrued expenses	157,958	185,935
Total current liabilities	460,785	467,781
LONG-TERM DEBT, less current portion	2,341,563	2,303,442
DEFERRED INCOME TAX LIABILITIES, net	852,731	873,194
DEFERRED ITEMS - grants from outside parties	321,420	321,592
OTHER LONG-TERM LIABILITIES	170,901	172,796
COMMITMENTS AND CONTINGENCIES		
EQUITY:		
Class A Common Stock, \$0.01 par value, one vote per share; 180,000,000 shares authorized at March 31, 2018 and December 31, 2017; 74,924,202 and 74,808,305 shares issued and 61,229,743 and 61,946,078 shares outstanding (net of 13,694,459 and 12,862,227 shares in treasury) on March 31, 2018 and December 31, 2017, respectively	749	748
Class B Common Stock, \$0.01 par value, ten votes per share; 30,000,000 shares authorized at March 31, 2018 and December 31, 2017; 701,138 shares issued and outstanding on March 31, 2018 and December 31, 2017	7	7
Additional paid-in capital	1,762,437	1,757,332
Retained earnings	2,312,932	2,234,864
Accumulated other comprehensive loss	(98,159)	(105,534)
Treasury stock, at cost	(297,126)	(236,951)
Total Genesee & Wyoming Inc. stockholders' equity	3,680,840	3,650,466
Noncontrolling interest	242,536	245,626
Total equity	3,923,376	3,896,092
Total liabilities and equity	\$8,070,776	\$8,034,897

The accompanying notes are an integral part of these consolidated financial statements.

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GENESEE & WYOMING INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE THREE MONTHS ENDED MARCH 31, 2018 and 2017 (Unaudited)
(in thousands, except per share amounts)

	Three Months Ended March 31,	
	2018	2017
OPERATING REVENUES	\$574,661	\$519,108
OPERATING EXPENSES:		
Labor and benefits	183,716	167,138
Equipment rents	34,087	33,871
Purchased services	64,102	51,001
Depreciation and amortization	65,990	60,774
Diesel fuel used in train operations	46,151	38,153
Electricity used in train operations	2,234	3,173
Casualties and insurance	9,966	12,543
Materials	32,469	20,546
Trackage rights	20,978	22,223
Net gain on sale and impairment of assets	(1,036)	(427)
Restructuring costs	283	3,755
Other expenses	28,808	30,458
Total operating expenses	487,748	443,208
OPERATING INCOME	86,913	75,900
Interest income	498	227
Interest expense	(25,236)	(26,365)
Other loss, net	(2,040)	(545)
Income before income taxes	60,135	49,217
Benefit from/(provision for) income taxes	15,890	(21,928)
Net income	\$76,025	\$27,289
Less: Net income attributable to noncontrolling interest	927	1,051
Net income attributable to Genesee & Wyoming Inc.	\$75,098	\$26,238
Basic earnings per common share attributable to Genesee & Wyoming Inc. common stockholders:	\$1.21	\$0.43
Weighted average shares - Basic	61,918	61,413
Diluted earnings per common share attributable to Genesee & Wyoming Inc. common stockholders:	\$1.19	\$0.42
Weighted average shares - Diluted	62,887	62,353
The accompanying notes are an integral part of these consolidated financial statements.		

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GENESEE & WYOMING INC. AND SUBSIDIARIES
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
 FOR THE THREE MONTHS ENDED MARCH 31, 2018 and 2017 (Unaudited)
 (dollars in thousands)

	Three Months Ended March 31,	
	2018	2017
NET INCOME	\$76,025	\$27,289
OTHER COMPREHENSIVE INCOME:		
Foreign currency translation adjustment	(617)	36,253
Net unrealized gain on qualifying cash flow hedges, net of tax provision of (\$2,150) and (\$624), respectively	6,901	506
Changes in pension and other postretirement benefits, net of tax (provision)/benefit of (\$14) and \$449, respectively	43	(893)
Other comprehensive income	6,327	35,866
COMPREHENSIVE INCOME	\$82,352	\$63,155
Less: Comprehensive (loss)/income attributable to noncontrolling interest	(3,091)	13,086
COMPREHENSIVE INCOME ATTRIBUTABLE TO GENESEE & WYOMING INC.	\$85,443	\$50,069

The accompanying notes are an integral part of these consolidated financial statements.

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GENESEE & WYOMING INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE THREE MONTHS ENDED MARCH 31, 2018 and 2017 (Unaudited)
(dollars in thousands)

	Three Months Ended March 31,	
	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$76,025	\$27,289
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	65,990	60,774
Stock-based compensation	4,052	4,213
Deferred income taxes	(24,148)	13,572
Net gain on sale and impairment of assets	(1,036)	(427)
Changes in assets and liabilities which provided/(used) cash, net of effect of acquisitions:		
Accounts receivable, net	(6,299)	6,524
Materials and supplies	2,593	(2,140)
Prepaid expenses and other	(7,025)	(2,226)
Accounts payable and accrued expenses	(12,381)	(29,330)
Other assets and liabilities, net	3,588	6,767
Net cash provided by operating activities	101,359	85,016
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(58,222)	(34,738)
Grant proceeds from outside parties	5,934	4,771
Net cash provided by acquisitions	—	2,935
Insurance proceeds for the replacement of assets	1,600	1,406
Proceeds from disposition of property and equipment	1,423	928
Net cash used in investing activities	(49,265)	(24,698)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Principal payments on revolving line-of-credit, long-term debt and capital lease obligations	(121,850)	(167,730)
Proceeds from revolving line-of-credit and long-term borrowings	176,840	112,294
Common share repurchases	(57,376)	—
Installment payments on Freightliner deferred consideration	(6,255)	—
Other financing related activities, net	(1,973)	(814)
Net cash used in financing activities	(10,614)	(56,250)
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	(562)	1,878
INCREASE IN CASH AND CASH EQUIVALENTS	40,918	5,946
CASH AND CASH EQUIVALENTS, beginning of period	80,472	32,319
CASH AND CASH EQUIVALENTS, end of period	\$121,390	\$38,265

The accompanying notes are an integral part of these consolidated financial statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. PRINCIPLES OF CONSOLIDATION AND BASIS OF PRESENTATION:

The interim consolidated financial statements presented herein include the accounts of Genesee & Wyoming Inc. and its subsidiaries. All significant intercompany transactions and accounts have been eliminated in consolidation. These interim consolidated financial statements have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) and are unaudited. They do not contain all disclosures which would be required in a full set of financial statements prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP). In the opinion of management, the unaudited financial statements for the three months ended March 31, 2018 and 2017 are presented on a basis consistent with the audited financial statements and contain all adjustments, consisting only of normal recurring adjustments, necessary to provide a fair statement of the results for the interim periods presented. The results of operations for interim periods are not necessarily indicative of results of operations for the full year. The consolidated balance sheet data for 2017 was derived from the audited financial statements in the Company's 2017 Annual Report on Form 10-K, but does not include all disclosures required by U.S. GAAP.

The results of operations of the foreign entities are maintained in the local currency of the respective subsidiary and translated into United States dollars at the applicable exchange rates for inclusion in the consolidated financial statements. As a result, any appreciation or depreciation of these currencies against the United States dollar will impact the Company's results of operations.

The interim consolidated financial statements should be read in conjunction with the audited financial statements and notes thereto for the year ended December 31, 2017 included in the Company's 2017 Annual Report on Form 10-K. Certain reclassifications and adjustments have been made to prior period balances to conform to the current year presentation as noted below:

On January 1, 2018, the Company adopted ASU 2017-07, Compensation-Retirement Benefits (Topic 715), Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. Prior to the adoption of ASU 2017-07, the Company presented net pension costs within operating income on the same line item as other compensation costs arising from services rendered by the applicable employees. ASU 2017-07 requires that net pension costs, other than service cost, be presented outside of operating income. The Company applied these changes retrospectively to its consolidated statement of operations for the three months ended March 31, 2017, which resulted in a decrease in operating income of \$1.6 million and a corresponding decrease in other loss, net. The adjustment had no impact on net income.

On January 1, 2018, the Company adopted ASU 2018-02, Income Statement - Reporting Comprehensive Income (Topic 220), Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. The current standard, ASC Topic 740, requires deferred tax liabilities to be adjusted for the effect of a change in tax laws or rates with the effect included in income from operations in the reporting period of the enactment date. The Tax Cuts and Jobs Act of 2017 (the TCJA) enacted by the United States federal government resulted in tax effects of items recorded within accumulated other comprehensive income (AOCI) to be "stranded," as those items no longer reflect the appropriate tax rate. This amendment allows the reclassification from AOCI to retained earnings for the stranded tax effects resulting from the new income tax rates. The Company applied the amendments as of January 1, 2018 by reclassifying \$3.0 million from AOCI to retained earnings, eliminating the stranded tax effects in AOCI resulting from the TCJA. This reclassification reduced AOCI and increased retained earnings by \$3.0 million. It is the Company's policy to release income tax effects from accumulated other comprehensive loss using the item-by-item approach.

On January 1, 2018, the Company adopted ASU 2014-09, Revenue from Contracts with Customers, which supersedes previous revenue guidance. The standard requires that the Company recognize revenue when it transfers the promised goods or services to customers in an amount that reflects the consideration the Company expects to receive in exchange for those goods or services. The Company adopted ASU 2014-09 and all related amendments using the modified retrospective approach. Under the standard, the Company continues to recognize freight revenue proportionally as a shipment moves from origin to destination. The adoption did not affect the Company's financial

condition, results of operations or liquidity. Disclosures related to the nature, amount and timing of revenue and cash flows resulting from contracts with customers are included in Note 4, Revenue.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

On December 1, 2016, a subsidiary of the Company completed the acquisition of Glencore Rail (NSW) Pty Limited (GRail) and concurrently issued a 48.9% stake in G&W Australia Holdings LP (GWAHLP) (collectively, the Australia Partnership), which is the holding entity for all of the Company's Australian businesses, including GRail, to a consortium of funds and clients managed by Macquarie Infrastructure and Real Assets (MIRA), a large infrastructure investment firm. The Company, through wholly-owned subsidiaries, also made incremental investments and retained a 51.1% ownership in GWAHLP. The investments made by both the Company and MIRA consisted of equity and debt financing of GWAHLP in similar proportions. As MIRA's investments were made at the contemporaneous fair value of GWAHLP as of December 1, 2016, accounting for MIRA's noncontrolling interest in the Company's consolidated financial statements required adjustments to reflect a proportional interest in the net book value of GWAHLP. During the three months ended March 31, 2018, the Company determined that there was an error in its December 1, 2016 calculation of the noncontrolling interest for MIRA's 48.9% equity interest, which resulted in the following adjustment within the total equity section of the Company's consolidated balance sheet: a decrease in noncontrolling interest of \$71.9 million, an increase in additional paid-in capital of \$57.9 million and a decrease in accumulated other comprehensive loss of \$14.0 million. This revision has been reflected in the Company's consolidated balance sheet as of December 31, 2017 as well as the December 31, 2016 equity balances as disclosed in Note 12, Stockholders' Equity. There was no effect on any other section of the Company's balance sheet. This revision had no impact on the Company's consolidated statements of operations, comprehensive income or cash flows for the three months ended March 31, 2018 or 2017. The Company does not consider this revision material to any previously issued consolidated financial statements.

When comparing the Company's results of operations from one reporting period to another, it is important to consider that the Company has historically experienced fluctuations in revenues and expenses due to acquisitions, changing economic conditions, fluctuations in commodity prices, competitive forces, changes in foreign currency exchange rates, rail network congestion, one-time freight moves, fuel price fluctuations, customer plant expansions and shutdowns, sales of property and equipment, derailments and weather-related conditions, such as hurricanes, cyclones, tornadoes, high winds, droughts, heavy snowfall, unseasonably hot or cold weather, freezing and flooding, among other factors. In periods when these events occur, the Company's results of operations are not easily comparable from one period to another. Finally, certain of the Company's railroads have commodity shipments that are sensitive to general economic conditions, global commodity prices and foreign exchange rates, such as steel products, iron ore, paper products, lumber and forest products and agricultural products, as well as product specific market conditions, such as the availability of lower priced alternative sources of power generation (coal) and energy commodity price differentials (crude oil and natural gas liquids) or congestion at ports (intermodal). Other shipments are relatively less affected by economic conditions and are more closely affected by other factors, such as winter weather (salt) and seasonal rainfall (agricultural products). As a result of these and other factors, the Company's results of operations in any reporting period may not be directly comparable to the Company's results of operations in other reporting periods.

2. CHANGES IN OPERATIONS:

North American Operations

Heart of Georgia Railroad, Inc.: On May 31, 2017, the Company completed the acquisition of all the outstanding shares of Atlantic Western Transportation, Inc., the parent company of Heart of Georgia Railroad, Inc. (HOG), for \$5.6 million in cash and contingent consideration valued at \$5.7 million. The contingent consideration is payable to the sellers upon satisfaction of certain conditions, which the Company expects to be paid in 2021. The results of operations from HOG have been included in the Company's consolidated statements of operations since the acquisition date.

HOG was founded in 1999 and operates 219 miles of track that runs across the State of Georgia. The track is leased from the Georgia Department of Transportation. It connects with the Company's Georgia Southwestern Railroad at Americus, Georgia, and with the Company's Georgia Central Railway at Vidalia, Georgia. HOG serves an inland intermodal terminal at Cordele, Georgia, providing five days per week, direct rail service via the Georgia Central Railway to the Port of Savannah for auto, agricultural products and other merchandise customers. HOG has Class I

railroad connections with CSX Corp. at Cordele and with Norfolk Southern at Americus and Helena, Georgia. HOG transports approximately 10,000 annual carloads of agricultural products, feed, fertilizer, and lumber and forest products, of which approximately 2,000 carloads are interchanged with the Company's Georgia Central Railway.

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 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

U.K./European Operations

Pentalver Transport Limited: On May 3, 2017, the Company's subsidiary, GWI UK Acquisition Company Limited, purchased for cash all of the issued share capital of Pentalver Transport Limited (Pentalver) from a subsidiary of APM Terminals (a subsidiary of A P Møller-Maersk A/S) for £97.8 million (or \$126.2 million at the exchange rate on May 3, 2017) or £77.5 million (or \$100.1 million at the exchange rate on May 3, 2017) net of £20.2 million (or \$26.1 million at the exchange rate on May 3, 2017) of cash received in connection with the sale. The Company funded the acquisition with borrowings under the Company's Second Amended and Restated Senior Secured Syndicated Credit Facility Agreement (the Credit Agreement). The foreign exchange rate used to translate the total consideration to United States dollars was \$1.29 for one British pound.

Headquartered in Southampton, U.K., Pentalver operates off-dock container terminals (most under long-term leases) strategically placed at each of the four major seaports of Felixstowe, Southampton, London Gateway and Tilbury, as well as an inland terminal located at Cannock, in the Midlands, near many of the nation's largest distribution centers. In addition to providing storage for loaded and empty containers on over 100 acres of land, Pentalver also operates a trucking haulage service with more than 150 trucks, primarily providing daily service between the seaports of Felixstowe and Southampton and its inland terminal at Cannock. Pentalver also provides services related to container maintenance and repair (including refrigerated containers) and is one of the largest sellers of new and used containers in the U.K.

Pentalver's operations are complementary to those of the Company's Freightliner Group Limited (Freightliner) subsidiary, which is the largest rail maritime intermodal operator in the U.K. The logistics of maritime container transportation in the U.K. are highly competitive, whether by road, rail or short-sea, with a premium placed on timely, efficient and safe service. The results of operations from Pentalver have been included in the Company's consolidated statements of operations since the May 3, 2017 acquisition date.

The Company accounted for the acquisition as a business combination using the acquisition method of accounting under U.S. GAAP. The acquired assets and liabilities of Pentalver were recorded at their acquisition-date fair values and were consolidated with those of the Company as of the acquisition date. The foreign exchange rate used to translate the balance sheet to United States dollars was \$1.29 for one British pound.

The acquisition date fair values were assigned to the acquired net assets as follows (amounts in thousands):

	GBP	USD
Cash and cash equivalents	£20,224	\$26,117
Accounts receivable	16,849	21,759
Materials and supplies	13,360	17,253
Prepaid expenses and other	3,238	4,182
Property and equipment	20,649	26,666
Goodwill	8,592	