TREX CO INC
Form 10-Q
May 05, 2014
Table of Contents

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, 2014

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	**54-1910453**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
160 Exeter Drive Winchester, Virginia	**22603-8605**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (540) 542-6300

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 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 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 ¨	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 x

The number of shares of the registrant s common stock, par value $.01 per share, outstanding at April 21, 2014 was 16,797,224 shares.

Table of Contents

TREX COMPANY, INC.

INDEX

Table of Contents

PART I

FINANCIAL INFORMATION

Item 1. Financial Statements

TREX COMPANY, INC.

Condensed Consolidated Balance Sheets

(In thousands)

	March 31, 2014 (Unaudited)	December 31, 2013
Assets		
Current assets:		
Cash and cash equivalents	$ 3,729	$ 3,772
Accounts receivable, net	116,470	37,338
Inventories	30,213	22,428
Prepaid expenses and other assets	2,969	3,145
Deferred income taxes	9,145	9,497
Total current assets	162,526	76,180
Property, plant, and equipment, net	100,278	100,783
Goodwill and other intangibles	10,539	10,542
Other assets	652	652
Total assets	$ 273,995	$ 188,157
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 10,999	$ 14,891
Accrued expenses	16,478	23,295
Accrued warranty	9,000	9,000
Line of credit	80,000	
Total current liabilities	116,477	47,186
Deferred income taxes	360	360
Non-current accrued warranty	29,802	31,812
Other long-term liabilities	2,134	2,183
Total liabilities	148,773	81,541
Stockholders equity:		

Preferred stock, $0.01 par value, 3,000,000 shares authorized; none issued and outstanding		
Common stock, $0.01 par value, 40,000,000 shares authorized; 17,339,036 and 17,299,062 shares issued and 16,777,781 and 16,737,807 shares outstanding at March 31, 2014 and December 31, 2013, respectively	173	173
Additional paid-in capital	107,978	101,667
Retained earnings	42,071	29,776
Treasury stock, at cost, 561,255 shares	(25,000)	(25,000)
Total stockholders equity	125,222	106,616
Total liabilities and stockholders equity	$ 273,995	$ 188,157

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, 2014	Three Months Ended March 31, 2013
Net sales	$ 100,645	$ 107,880
Cost of sales	62,478	66,020
Gross profit	38,167	41,860
Selling, general and administrative expenses	18,222	19,842
Income from operations	19,945	22,018
Interest expense, net	323	251
Income before income taxes	19,622	21,767
Provision for income taxes	7,327	198
Net income	$ 12,295	$ 21,569
Basic earnings per common share	$ 0.74	$ 1.28
Basic weighted average common shares outstanding	16,564,338	16,883,111
Diluted earnings per common share	$ 0.73	$ 1.25
Diluted weighted average common shares outstanding	16,799,719	17,280,445
Comprehensive income	$ 12,295	$ 21,569

See Accompanying Notes to Condensed Consolidated

Financial Statements (Unaudited).

2

Table of Contents

TREX COMPANY, INC.

Condensed Consolidated Statements of Cash Flows

(Unaudited)

(In thousands)

	Three Months Ended March 31,	
	2014	**2013**
Operating Activities		
Net income	$ 12,295	$ 21,569
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	3,797	4,164
Stock-based compensation	1,170	895
Deferred income taxes	352	(237)
Gain on disposal of property, plant and equipment	(37)	(67)
Excess tax benefits from stock compensation	(6,507)	
Changes in operating assets and liabilities:		
Accounts receivable	(79,152)	(90,840)
Inventories	(7,785)	2,487
Prepaid expenses and other assets	(82)	850
Accounts payable	(3,892)	1,874
Accrued expenses and other liabilities	(9,068)	(7,004)
Income taxes receivable/payable	6,884	356
Net cash used in operating activities	(82,025)	(65,953)
Investing Activities		
Expenditures for property, plant and equipment	(3,188)	(1,910)
Proceeds from sales of property, plant and equipment	37	67
Purchase of acquired company, net of cash acquired	(44)	
Notes receivable, net	19	31
Net cash used in investing activities	(3,176)	(1,812)
Financing Activities		
Financing costs		(73)
Borrowings under line of credit	85,000	67,000
Principal payments under line of credit	(5,000)	
Repurchases of common stock	(1,433)	(1,996)
Proceeds from employee stock purchase and option plans	84	2,577
Excess tax benefits from stock compensation	6,507	

Net cash provided by financing activities	85,158	67,508
Net decrease in cash and cash equivalents	(43)	(257)
Cash and cash equivalents at beginning of period	3,772	2,159
Cash and cash equivalents at end of period	$ 3,729	$ 1,902
Supplemental Disclosure:		
Cash paid for interest, net of capitalized interest	$ 99	$ 96
Cash paid for income taxes, net	$ 91	$ 79

See Accompanying Notes to Condensed Consolidated

Financial Statements (Unaudited).

3

Table of Contents

TREX COMPANY, INC.

Notes to Condensed Consolidated Financial Statements

For the Three Months Ended March 31, 2014 and 2013

(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) considered necessary for a fair presentation have been included in the accompanying condensed consolidated financial statements. Certain prior year amounts in the accompanying condensed consolidated financial statements have been reclassified to conform to the current year presentation. The consolidated results of operations for the three months ended March 31, 2014 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, 2013 and 2012 and for each of the three years in the period ended December 31, 2013 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, 2013.

3. INVENTORIES

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

	March 31, 2014	December 31, 2013
Finished goods	$ 39,339	$ 30,423
Raw materials	15,371	16,502
Total FIFO inventories	54,710	46,925
Reserve to adjust inventories to LIFO value	(24,497)	(24,497)

Total LIFO inventories	$ 30,213	$ 22,428

Under the LIFO method, reductions in inventory cause a portion of the Company s cost of sales to be based on historical costs rather than current year costs. There were no LIFO inventory liquidations in the three months ended March 31, 2014 or 2013.

An actual valuation of inventory under the LIFO method can be made only at the end of each year based on the inventory levels and costs at that time. Accordingly, interim LIFO calculations are based on management s estimates of expected year-end inventory levels and costs. Since inventory levels and costs are subject to factors beyond management s control, interim results are subject to the final year-end LIFO inventory valuation.

Table of Contents

4. ACCRUED EXPENSES

Accrued expenses consist of the following (in thousands):

	March 31, 2014	December 31, 2013
Accrued sales and marketing	$ 4,157	$ 5,269
Accrued compensation and benefits	3,919	9,135
Accrued rent obligations	2,227	1,787
Accrued legal contingency	1,586	3,174
Accrued manufacturing expenses	1,434	1,107
Other	3,155	2,823
Total accrued expenses	$ 16,478	$ 23,295

5. DEBT

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

Revolving Credit Facility

The Company currently has an Amended Credit Agreement which provides the Company with one or more revolving loans in a collective maximum principal amount of $100 million. On December 17, 2013, the Company entered into a Second Amendment (Second Amendment) to the Amended Credit Agreement dated as of January 6, 2012, as amended by the First Amendment dated February 26, 2013 (the Credit Agreement). Pursuant to the Second Amendment, the Credit Agreement was amended to temporarily increase the maximum amount of the Revolver Loans from $100 million to $125 million during the period from January 1, 2014 through and including June 30, 2014 to meet seasonal cash requirements. No other material changes were made to the terms of the Credit Agreement.

Amounts drawn under the Credit Agreement are subject to a borrowing base consisting of certain accounts receivables, inventories, machinery and equipment and real estate. At March 31, 2014, the Company had $80 million of outstanding borrowings under its revolving credit facility and remaining available borrowing capacity of approximately $45 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, 2014, 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.

6. 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, 2014 and December 31, 2013.

Table of Contents

7. 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, 2014	2013
Numerator:		
Net income available to common shareholders	$ 12,295	$ 21,569
Denominator:		
Basic weighted average shares outstanding	16,564,338	16,883,111
Effect of dilutive securities:		
SARs and options	151,457	330,075
Restricted stock	83,924	67,259
Diluted weighted average shares outstanding	16,799,719	17,280,445
Basic earnings per share	$ 0.74	$ 1.28
Diluted earnings per share	$ 0.73	$ 1.25

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, 2014	2013
Restricted stock and stock options	44	32,872
Stock appreciation rights	598	30,753

Stock Repurchase Programs

On October 24, 2013, the Company s Board of Directors authorized a common stock repurchase program, expiring on February 10, 2014, of up to $30 million of the Company s outstanding common stock (the October 2013 Stock Repurchase Program). The Company made no repurchases under the October 2013 Stock Repurchase Program before it expired.

On February 19, 2014, the Company s Board of Directors authorized an additional common stock repurchase program of up to $50 million of the Company s outstanding common stock (the February 2014 Stock Repurchase Program).

This authorization has no expiration date. During the three months ended March 31, 2014, the Company made no repurchases under the February 2014 Stock Repurchase Program.

8. STOCK-BASED COMPENSATION

As of March 31, 2014, the Company has one stock-based compensation plan, the 2005 Stock Incentive Plan (the 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, stock appreciation rights (SARs), restricted stock and performance share awards. As of March 31, 2014, the total aggregate number of shares of the Company s common stock that may be issued under the Plan is 3,150,000.

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.

Table of Contents

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, 2014 and 2013, respectively, the assumptions shown in the following table were used:

	Three Months Ended March 31, 2014	2013
Weighted-average fair value of grants	$ 37.40	$ 23.34
Dividend yield	0%	0%
Average risk-free interest rate	1.8%	0.7%
Expected term (years)	5	5
Expected volatility	54%	64%

The following table summarizes the Company s stock-based compensation grants for the three months ended March 31, 2014:

	Stock Awards Granted	Weighted-Average Grant Price Per Share
Stock appreciation rights	1,562	$ 78.15
Time-based restricted stock	27,062	$ 67.45
Performance-based restricted stock	21,338	$ 67.43

The Company recognizes stock-based compensation expense ratably over the period from 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, 2014 and 2013 (in thousands):

	Three Months Ended March 31, 2014	2013
Stock appreciation rights	$ 370	$ 331
Time-based restricted stock	708	537