SCHOLASTIC CORP
Form 10-Q
January 09, 2008

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 the quarterly period ended November 30, 2007 — Commission File No. 000-19860

SCHOLASTIC CORPORATION
(Exact name of Registrant as specified in its charter)

Delaware	**13-3385513**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
557 Broadway, New York, New York	**10012**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code (212) 343-6100

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 o

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x Accelerated filer o Non-accelerated filer o

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

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

Title of each class	Number of shares outstanding as of December 31, 2007
Common Stock, $.01 par value	36,805,947
Class A Stock, $.01 par value	1,656,200

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

SCHOLASTIC CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS - UNAUDITED
(Dollar amounts in millions, except per share data)

	Three months ended November 30,		*Six months ended November 30,*	
	2007	**2006**	**2007**	**2006**
Revenues	**$ 746.2**	**$ 735.5**	**$ 1,333.1**	**$ 1,070.4**
Operating costs and expenses:				
Cost of goods sold	318.1	323.1	642.6	494.9
Selling, general and administrative expenses	264.1	250.5	486.8	447.1
Bad debt expense	17.5	19.5	35.3	35.2
Depreciation and amortization	16.3	16.0	33.0	32.9
Total operating costs and expenses	616.0	609.1	1,197.7	1,010.1
Operating income	**130.2**	**126.4**	**135.4**	**60.3**
Interest expense, net	9.5	8.3	17.9	15.7
Earnings before income taxes	120.7	118.1	117.5	44.6
Provision for income taxes	45.1	43.0	44.7	16.4
Net income	**$ 75.6**	**$ 75.1**	**$ 72.8**	**$ 28.2**
Basic and diluted earnings per Share of Class A and Common Stock:				
Basic	$ 1.96	$ 1.77	$ 1.86	$ 0.67
Diluted	$ 1.93	$ 1.75	$ 1.83	$ 0.66

See accompanying notes

SCHOLASTIC CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(Dollar amounts in millions, except per share data)

	November 30, 2007	May 31, 2007	November 30, 2006
	(Unaudited)		*(Unaudited)*
ASSETS			
Current Assets:			
Cash and cash equivalents	$ 187.6	$ 22.8	$ 133.7
Accounts receivable, net	343.0	281.6	339.0
Inventories	478.1	422.9	494.3
Deferred promotion costs	51.4	50.1	65.5
Deferred income taxes	93.3	71.5	73.9
Prepaid expenses and other current assets	59.3	55.8	48.8
Total current assets	1,212.7	904.7	1,155.2
Property, plant and equipment, net	377.0	383.3	386.2
Prepublication costs	115.0	112.7	109.0
Installment receivables, net	12.7	13.1	9.1
Royalty advances	51.7	51.3	48.4
Production costs	4.8	4.3	5.1
Goodwill	265.3	265.9	254.2
Other intangibles	78.4	78.5	78.6
Other assets and deferred charges	59.9	63.9	65.0
Total assets	**$ 2,177.5**	**$ 1,877.7**	**$ 2,110.8**
LIABILITIES AND STOCKHOLDERS EQUITY			
Current Liabilities:			
Lines of credit, short-term debt and current portion of long-term debt	$ 83.3	$ 66.2	$ 303.9
Capital lease obligations	5.2	5.5	5.7
Accounts payable	146.5	135.4	145.6
Accrued royalties	143.1	39.2	42.9
Deferred revenue	63.7	24.2	54.3
Other accrued expenses	190.2	143.6	162.5
Total current liabilities	632.0	414.1	714.9
Noncurrent Liabilities:			
Long-term debt	330.8	173.4	173.3
Capital lease obligations	58.5	59.8	60.4
Other noncurrent liabilities	127.6	101.4	77.8
Total noncurrent liabilities	516.9	334.6	311.5
Commitments and Contingencies			
Stockholders Equity:			
Preferred Stock, $1.00 par value			

Class A Stock, $.01 par value	0.0	0.0	0.0
Common Stock, $.01 par value	0.4	0.4	0.4
Additional paid-in capital	527.0	490.3	469.2
Accumulated other comprehensive loss	(38.0)	(34.5)	(25.3)
Retained earnings	739.2	672.8	640.1
Treasury stock at cost	(200.0)		
Total stockholders equity	1,028.6	1,129.0	1,084.4
Total liabilities and stockholders equity	**$ 2,177.5**	**$ 1,877.7**	**$ 2,110.8**

See accompanying notes

SCHOLASTIC CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS UNAUDITED
(Dollar amounts in millions)

	Six months ended November 30,	
	2007	**2006**
Cash flows provided by operating activities:		
Net income	$ 72.8	$ 28.2
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for losses on accounts receivable and other reserves	56.0	52.3
Amortization of prepublication and production costs	23.5	30.5
Depreciation and amortization	33.0	32.9
Royalty advances expensed	13.3	11.2
Deferred income taxes	(1.2)	(0.2)
Changes in assets and liabilities:		
Accounts receivable	(91.5)	(103.0)
Inventories	(68.7)	(77.1)
Prepaid expenses and other current assets	0.4	3.7
Deferred promotion costs	(0.9)	(15.6)
Accounts payable and other accrued expenses	55.3	9.7
Accrued royalties	103.4	6.2
Deferred revenue	40.6	34.8
Other, net	(1.4)	(2.9)
Total adjustments	161.8	(17.5)
Net cash provided by operating activities	234.6	10.7
Cash flows used in investing activities:		
Prepublication expenditures	(24.5)	(20.4)
Additions to property, plant and equipment	(22.6)	(19.3)
Royalty advances	(15.9)	(14.9)
Production expenditures	(2.1)	(2.5)
Repayment of loan from investee	6.2	5.7
Loan to investee		(1.9)
Other	(0.3)	(1.8)
Net cash used in investing activities	(59.2)	(55.1)
Cash flows provided by (used in) financing activities:		
Borrowings under Credit Agreement, Revolver and Revolving Loan	190.0	116.0
Repayments of Credit Agreement, Revolver and Revolving Loan	(190.0)	(116.0)
Borrowings under Term Loan	200.0	
Repurchase of 5.75% Notes		(36.0)
Borrowings under lines of credit	356.0	101.0
Repayments of lines of credit	(383.0)	(89.4)
Repayments of capital lease obligations	(2.9)	(4.6)
Reacquisition of Common Stock	(200.0)	
Proceeds pursuant to stock-based compensation plans	30.6	11.0
Other	0.7	(0.1)
Net cash provided by (used in) financing activities	1.4	(18.1)

Effect of exchange rate changes on cash and cash equivalents	(12.0)	(9.1)
Net increase (decrease) in cash and cash equivalents	164.8	(71.6)
Cash and cash equivalents at beginning of period	22.8	205.3
Cash and cash equivalents at end of period	**$ 187.6**	**$ 133.7**

See accompanying notes

SCHOLASTIC CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS UNAUDITED
(Dollar amounts in millions, except per share data)

1. Basis of Presentation

The accompanying condensed consolidated financial statements consist of the accounts of Scholastic Corporation (the Corporation) and all wholly-owned and majority-owned subsidiaries (collectively, Scholastic or the Company). These financial statements have not been audited but reflect those adjustments consisting of normal recurring items that management considers necessary for a fair presentation of financial position, results of operations and cash flows. These financial statements should be read in conjunction with the consolidated financial statements and related notes in the Annual Report on Form 10-K for the fiscal year ended May 31, 2007.

The Company s business is closely correlated to the school year. Consequently, the results of operations for the three and six months ended November 30, 2007 and 2006 are not necessarily indicative of the results expected for the full year. Due to the seasonal fluctuations that occur, the November 30, 2006 condensed consolidated balance sheet is included for comparative purposes.

The Company s condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States and with the instructions to Form 10-Q and Regulation S-X. The preparation of these financial statements involves the use of estimates and assumptions by management, which affect the amounts reported in the condensed consolidated financial statements and accompanying notes. The Company bases its estimates on historical experience, current business factors, and various other assumptions believed to be reasonable under the circumstances, all of which are necessary in order to form a basis for determining the carrying values of assets and liabilities. Actual results may differ from those estimates and assumptions. On an ongoing basis, the Company evaluates the adequacy of its reserves and the estimates used in calculations, including, but not limited to: collectability of accounts receivable and installment receivables; sales returns; amortization periods; pension and other post-retirement obligations; tax rates; and recoverability of inventories, deferred promotion costs, deferred income taxes and tax reserves, prepublication costs, royalty advances, goodwill and other intangibles.

Certain prior year amounts have been reclassified to conform to the current year presentation. The Company had previously reported certain amounts related to the translation of foreign currency amounts in Other, net in the Statement of Cash Flows that are now presented as a component of the Effect of exchange rate changes on cash and cash equivalents. The prior year reclassifications to the Statement of Cash Flows resulted in a $6.3 increase in Net cash provided by operating activities for the six months ended November 30, 2006, of which $9.7 was attributable to the foreign currency reclassification, offset primarily by a $3.8 reclassification of a related party loan to Net cash used in investing activities.

New Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 157, Fair Value Measurements (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157 emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and states that a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. SFAS 157 will become effective for the Company s fiscal year beginning June 1, 2008. The Company is currently evaluating the impact, if any, that SFAS 157 will have on its consolidated financial position, results of operations and cash flows.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS 159), to provide companies with an option to report selected financial assets and liabilities at fair value. The objective of SFAS 159 is to reduce both the complexity in accounting for financial instruments and the volatility in earnings caused by measuring related assets and liabilities differently. SFAS 159 will become effective for the Company s fiscal year beginning June 1, 2008. The Company is currently evaluating the impact, if any, that SFAS 159 will have on its consolidated financial position, results of operations and cash flows.

In December 2007, the FASB issued SFAS No. 141 (revised), Business Combinations (SFAS 141R). SFAS 141R establishes principles and requirements for how an acquiror accounts for business combinations. SFAS 141R includes guidance for the recognition and measurement of the identifiable assets acquired, the liabilities assumed, and any noncontrolling or minority interest in the acquiree. It also provides guidance for the measurement of goodwill, the recognition of contingent consideration, the accounting for pre-acquisition gain and loss contingencies and acquisition-related transaction costs, and the recognition of changes in the acquiror s income tax valuation allowance. SFAS 141R applies prospectively and is effective for business combinations made by the Company beginning June 1, 2009.

In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51, (SFAS 160). SFAS 160 amends Accounting Research Bulletin No. 51, Consolidated Financial Statements, to establish accounting and reporting standards for any noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS 160 clarifies that a noncontrolling interest in a subsidiary should be reported as a component of equity in the consolidated financial statements and requires disclosure, on the face of the consolidated statement of income, of the amounts of consolidated net income attributable to the parent and to the noncontrolled interest. SFAS 160 is effective for the Company beginning June 1, 2009 and is to be applied prospectively, except for the presentation and disclosure requirements, which upon adoption will be applied retrospectively for all periods presented. The Company is currently evaluating the impact, if any, that SFAS 160 will have on its consolidated financial position, results of operations and cash flows.

SCHOLASTIC CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS UNAUDITED
(Dollar amounts in millions, except per share data)

2. Segment Information

The Company categorizes its businesses into four operating segments: *Children s Book Publishing and Distribution; Educational Publishing; Media, Licensing and Advertising* (which collectively represent the Company s domestic operations)*;* and *International*. This classification reflects the nature of products and services consistent with the method by which the Company s chief operating decision-maker assesses operating performance and allocates resources. Revenues and operating margin related to a segment s products sold or services rendered through another segment s distribution channel are reallocated to the segment originating the products or services.

Children s Book Publishing and Distribution includes the publication and distribution of children s books in the United States through school-based book clubs and book fairs, school-based and direct-to-home continuity programs and the trade channel.

Educational Publishing includes the production and/or publication and distribution to schools and libraries of educational technology products, curriculum materials, children s books, classroom magazines and print and on-line reference and non-fiction products for grades pre-kindergarten to 12 in the United States.

Media, Licensing and Advertising includes the production and/or distribution of media and electronic products and programs (including children s television programming, videos, DVDs, software, feature films, interactive and audio products, promotional activities and non-book merchandise); and advertising revenue, including sponsorship programs.

International includes the publication and distribution of products and services outside the United States by the Company s international operations, and its export and foreign rights businesses.

The following table sets forth information for the Company s segments for the periods indicated:

	Children s Book Publishing and Distribution	Educational Publishing	Media, Licensing and Advertising	Overhead(1)	Total Domestic	International	Consolidated
Three months ended November 30, 2007							
Revenues	$ 431.3	$ 99.6	$ 57.7	$ 0.0	$ 588.6	$ 157.6	$ 746.2
Bad debt	14.8	0.4	0.0	0.0	15.2	2.3	17.5
Depreciation and amortization(2)	3.8	0.9	5.5	4.1	14.3	2.0	16.3
Amortization(3)	2.7	5.7	1.6	0.0	10.0	0.6	10.6
Royalty advances expensed	3.5	0.1	0.2	0.0	3.8	1.4	5.2
Operating income (loss)	99.7	12.5	10.9	(17.1)	106.0	24.2	130.2
Expenditures for long-lived assets(4)	9.4	6.8	5.9	7.2	29.3	5.2	34.5
Three months ended November 30, 2006							
Revenues	$ 442.7	$ 97.2	$ 56.6	$ 0.0	$ 596.5	$ 139.0	$ 735.5
Bad debt	14.5	0.6	1.2	0.0	16.3	3.2	19.5
Depreciation and amortization(2)	4.1	0.9	3.6	5.9	14.5	1.5	16.0
Amortization(3)	4.5	7.7	2.3	0.0	14.5	0.5	15.0
Royalty advances expensed	5.9	0.4	0.4	0.0	6.7	0.6	7.3
Operating income (loss)	99.6	17.1	9.2	(19.3)	106.6	19.8	126.4

Expenditures for long-lived assets(4)	16.2	6.8	4.5	3.8	31.3	3.4	34.7

(1) *Overhead includes all domestic corporate amounts not allocated to reportable segments, including expenses and costs related to the management of corporate assets. Unallocated assets are principally comprised of deferred income taxes and property, plant and equipment related to the Company s headquarters in the metropolitan New York area, its fulfillment and distribution facilities located in Missouri and Arkansas, and an industrial/office building complex in Connecticut.*

(2) *Includes depreciation of property, plant and equipment and amortization of intangible assets, but excludes amortization of promotion costs.*

(3) *Includes amortization of prepublication costs and production costs, but excludes amortization of promotion costs.*

(4) *Includes expenditures for property, plant and equipment, investments in prepublication and production costs, royalty advances and acquisitions of, and investments in, businesses.*

SCHOLASTIC CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - UNAUDITED
(Dollar amounts in millions, except per share data)

	Children s Book Publishing and Distribution	Educational Publishing	Media, Licensing and Advertising	Overhead (1)	Total Domestic	International	Consolidated
Six months ended November 30, 2007							
Revenues	$ 773.8	$ 227.4	$ 74.7	$ 0.0	$ 1,075.9	$ 257.2	$ 1,333.1
Bad debt	29.7	0.4	0.4	0.0	30.5	4.8	35.3
Depreciation and amortization(2)	8.5	1.9	5.8	12.9	29.1	3.9	33.0
Amortization(3)	7.2	12.1	3.1	0.0	22.4	1.1	23.5
Royalty advances expensed	13.3	0.6	0.3	0.0	14.2	1.6	15.8
Operating income (loss)	102.4	43.1	5.8	(37.4)	113.9	21.5	135.4
Segment assets	957.4	352.3	87.1	391.4	1,788.2	389.3	2,177.5
Goodwill	130.6	92.8	9.8	0.0	233.2	32.1	265.3
Expenditures for long-lived assets(4)	25.7	11.7	7.4	11.6	56.4	8.7	65.1
Long-lived assets(5)	299.5	211.5	37.4	264.2	812.6	119.4	932.0
Six months ended November 30, 2006							

