PRICESMART INC
Form 10-Q
July 09, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended May 31, 2012

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 0-22793

PriceSmart, Inc.
(Exact name of registrant as specified in its charter)

Delaware	33-0628530
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

9740 Scranton Road, San Diego, CA 92121
(Address of principal executive offices)

(858) 404-8800
(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 ý 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 ý 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. (Check one):

Large accelerated filer ¨ Accelerated filer ý 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 ý

The registrant had 30,204,353 shares of its common stock, par value $0.0001 per share, outstanding at June 30, 2012.

PRICESMART, INC.

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PART I—FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

PriceSmart, Inc.'s ("PriceSmart" or the "Company") unaudited consolidated balance sheet as of May 31, 2012 and the consolidated balance sheet as of August 31, 2011, the unaudited consolidated statements of income for the three and nine months ended May 31, 2012 and 2011, the unaudited consolidated statements of equity for the nine months ended May 31, 2012 and 2011, and the unaudited consolidated statements of cash flows for the nine months ended May 31, 2012 and 2011, are included herein. Also included herein are the notes to the unaudited consolidated financial statements.

PRICESMART, INC.
CONSOLIDATED BALANCE SHEETS
(AMOUNTS IN THOUSANDS, EXCEPT SHARE DATA)

	May 31, 2012 (Unaudited)	August 31, 2011
ASSETS		
Current Assets:		
Cash and cash equivalents	$104,943	$76,817
Short-term restricted cash	1,288	1,240
Receivables, net of allowance for doubtful accounts of $4 and $5 as of May 31, 2012 and August 31, 2011, respectively	4,323	3,655
Merchandise inventories	180,263	177,232
Deferred tax assets – current	4,897	4,252
Prepaid expenses and other current assets	28,743	29,117
Assets of discontinued operations	10	464
Total current assets	324,467	292,777
Long-term restricted cash	36,665	22,626
Property and equipment, net	289,700	281,111
Goodwill	37,104	37,361
Deferred tax assets – long term	14,947	17,000
Other non-current assets (includes $79 as of May 31, 2012 for the fair value of derivative instruments)	5,492	5,390
Investment in unconsolidated affiliates	7,565	8,063
Total Assets	$715,940	$664,328
LIABILITIES AND EQUITY		
Current Liabilities:		
Short-term borrowings	$2,169	$2,259
Accounts payable	164,756	163,432
Accrued salaries and benefits	13,590	11,681
Deferred membership income	13,079	11,416
Income taxes payable	8,107	7,655
Other accrued expenses	13,969	12,556
Dividends payable	9,063	—
Long-term debt, current portion	7,266	7,771
Deferred tax liability – current	378	533
Liabilities of discontinued operations	—	40
Total current liabilities	232,377	217,343
Deferred tax liability – long-term	1,624	1,888
Long-term portion of deferred rent	4,362	4,143
Long-term income taxes payable, net of current portion	2,618	3,310
Long-term debt, net of current portion	73,317	60,451
Other long-term liabilities (includes $914 and $884 for the fair value of derivative instruments and $606 and $471 for the defined benefit plan as of May 31, 2012 and August 31, 2011, respectively)	1,520	1,355
Total liabilities	315,818	288,490
Equity:		
Common stock, $0.0001 par value, 45,000,000 shares authorized; 30,847,734 and 30,695,933 shares issued and 30,204,353 and 29,900,030 shares outstanding (net of	3	3

treasury shares) as of May 31, 2012 and August 31, 2011, respectively		
Additional paid-in capital	382,570	383,549
Tax benefit from stock-based compensation	5,979	5,242
Accumulated other comprehensive loss	(32,121)	(22,915)
Retained earnings	60,030	28,238
Less: treasury stock at cost; 643,381 and 795,903 shares as of May 31, 2012 and August 31, 2011, respectively	(16,339)	(18,279)
Total equity	400,122	375,838
Total Liabilities and Equity	$715,940	$664,328

See accompanying notes.

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PRICESMART, INC.
CONSOLIDATED STATEMENTS OF INCOME
(UNAUDITED—AMOUNTS IN THOUSANDS, EXCEPT PER SHARE DATA)

	Three Months Ended		Nine Months Ended	
	May 31, 2012	May 31, 2011	May 31, 2012	May 31, 2011
Revenues:				
Net warehouse club sales	$494,898	$421,637	$1,501,043	$1,239,232
Export sales	2,768	1,890	8,476	5,170
Membership income	6,944	5,824	19,668	16,825
Other income	2,163	1,797	6,104	5,610
Total revenues	506,773	431,148	1,535,291	1,266,837
Operating expenses:				
Cost of goods sold:				
Net warehouse club	421,512	359,064	1,281,306	1,052,279
Export	2,622	1,804	8,075	4,906
Selling, general and administrative:				
Warehouse club operations	46,197	38,819	135,090	111,192
General and administrative	10,940	9,293	30,559	26,977
Pre-opening expenses	94	284	255	672
Total operating expenses	481,365	409,264	1,455,285	1,196,026
Operating income	25,408	21,884	80,006	70,811
Other income (expense):				
Interest income	279	300	668	667
Interest expense	(1,344)	(984)	(3,915)	(3,012)
Other income (expense), net	(538)	2,367	(975)	2,893
Total other expense	(1,603)	1,683	(4,222)	548
Income from continuing operations before provision for income taxes and loss of unconsolidated affiliates	23,805	23,567	75,784	71,359
Provision for income taxes	(8,078)	(7,199)	(25,854)	(22,093)
Income (loss) of unconsolidated affiliates	(19)	(3)	(9)	(45)
Income from continuing operations	15,708	16,365	49,921	49,221
Income (loss) from discontinued operations, net of tax	(2)	(75)	(6)	(161)
Net income	15,706	16,290	49,915	49,060
Net income per share available for distribution:				
Basic net income per share from continuing operations	$0.52	$0.55	$1.66	$1.65
Basic net income (loss) per share from discontinued operations, net of tax	$—	$—	$—	$—
Basic net income per share	$0.52	$0.55	$1.66	$1.65
Diluted net income per share from continuing operations	$0.52	$0.55	$1.66	$1.65
Diluted net income (loss) per share from discontinued operations, net of tax	$—	$—	$—	$—
Diluted net income per share	$0.52	$0.55	$1.66	$1.65
Shares used in per share computations:				
Basic	29,584	29,493	29,543	29,422

Diluted	29,595	29,502	29,555	29,430
Dividends per share	$—	$—	$0.60	$0.60

See accompanying notes.

PRICESMART, INC.
CONSOLIDATED STATEMENTS OF EQUITY
(UNAUDITED—AMOUNTS IN THOUSANDS)

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Tax Benefit From Stockbased Compensation	Accumulated Other Comprehensive Loss	Retained Earnings (Accumulated Deficit)	Treasury Stock Shares	Treasury Stock Amount	Total Equity
Balance at August 31, 2010	30,625	$3	$379,368	$ 4,490	$ (16,672)	$(15,578)	727	$(15,568)	$336,043
Purchase of treasury stock	—	—	—	—	—	—	67	(2,604)	(2,604)
Issuance of restricted stock awards	66	—	—	—	—	—	—	—	—
Forfeiture of restricted stock awards	(6)	—	—	—	—	—	—	—	—
Exercise of stock options	6	—	144	—	—	—	—	—	144
Stock-based compensation	—	—	3,076	876	—	—	—	—	3,952
Dividend payable to stockholders	—	—	—	—	—	(8,970)	—	—	(8,970)
Dividend paid to stockholders	—	—	—	—	—	(8,969)	—	—	(8,969)
Change in fair value of interest rate swaps	—	—	—	—	(23)	—	—	—	(23)
Net income	—	—	—	—	—	49,060	—	—	49,060
Translation adjustment	—	—	—	—	(396)	—	—	—	(396)
Comprehensive income									48,641
Balance at May 31, 2011	30,691	$3	$382,588	$ 5,366	$ (17,091)	$15,543	794	$(18,172)	$368,237
Balance at August 31, 2011	30,696	$3	$383,549	$ 5,242	$ (22,915)	$28,238	796	$(18,279)	$375,838
Purchase of treasury stock	—	—	—	—	—	—	44	(3,013)	(3,013)
Issuance of treasury stock	(197)	—	(4,953)	—	—	—	(197)	4,953	—
Issuance of restricted stock awards	345	—	—	—	—	—	—	—	—
Forfeiture of restricted stock awards	(2)	—	—	—	—	—	—	—	—

Exercise of stock options	6	—	89	—	—	—	—	—	89
Stock-based compensation	—	—	3,885	737	—	—	—	—	4,622
Dividend payable to stockholders	—	—	—	—	—	(9,063)	—	—	(9,063)
Dividend paid to stockholders	—	—	—	—	—	(9,060)	—	—	(9,060)
Change in fair value of interest rate swaps, net of tax	—	—	—	—	(33)	—	—	—	(33)
Amortization of prior service costs on defined benefit plan, net of tax	—	—	—	—	12	—	—	—	12
Net income	—	—	—	—	—	49,915	—	—	49,915
Translation adjustment to record merger of subsidiaries and correction to translation of Property and Equipment, net	—	—	—	—	(8,881)	—	—	—	(8,881)
Translation adjustment	—	—	—	—	(304)	—	—	—	(304)
Comprehensive income									40,709
Balance at May 31, 2012	30,848	$3	$382,570	$ 5,979	$ (32,121)	$60,030	643	$(16,339)	$400,122

See accompanying notes.

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PRICESMART, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED—AMOUNTS IN THOUSANDS)

	Nine Months Ended	
	May 31, 2012	May 31, 2011
Operating Activities:		
Net income	$49,915	$49,060
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	17,610	13,675
Allowance for doubtful accounts	(1)	(2)
(Gain) loss on sale of property and equipment	239	299
Gain on sale of excess real estate in Panama	—	(1,249)
Deferred income taxes	1,728	2,907
Discontinued operations	6	161
Excess tax deficiency (benefit) on stock-based compensation	(737)	(876)
Equity in gains/(losses) of unconsolidated affiliates	9	45
Stock-based compensation	3,885	3,076
Change in operating assets and liabilities:		
Change in receivables, prepaid expenses and other current assets, accrued salaries and benefits, deferred membership income and other accruals	4,625	(5,280)
Merchandise inventories	(3,031)	(36,497)
Accounts payable	1,326	13,355
Net cash provided by (used in) continuing operating activities	75,574	38,674
Net cash provided by (used in) discontinued operating activities	407	108
Net cash provided by (used in) operating activities	75,981	38,782
Investing Activities:		
Additions to property and equipment	(35,769)	(34,810)
Proceeds from disposal of property and equipment	86	37
Proceeds on sale of excess real estate in Panama	—	7,406
Net cash flows provided by (used in) investing activities	(35,683)	(27,367)
Financing Activities:		
Proceeds from bank borrowings	75,924	40,066
Repayment of bank borrowings	(63,397)	(32,176)
Release of (addition to) restricted cash	(14,000)	(14,920)
Cash dividend payments	(9,060)	(8,969)
Excess tax (deficiency) benefit on stock-based compensation	737	876
Purchase of treasury stock	(3,013)	(2,604)
Proceeds from exercise of stock options	89	144
Net cash provided by (used in) financing activities	(12,720)	(17,583)
Effect of exchange rate changes on cash and cash equivalents	548	(1,332)
Net increase (decrease) in cash and cash equivalents	28,126	(7,500)
Cash and cash equivalents at beginning of period	76,817	73,346
Cash and cash equivalents at end of period	$104,943	$65,846
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Interest, net of amounts capitalized	$3,775	$2,767
Income taxes	$22,193	$16,130
Supplemental non-cash item:		

Cancellation of joint ventures Prico Enterprise loan	$(473)	$—
Dividends declared but not paid	$9,063	$8,970

PRICESMART, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
May 31, 2012

NOTE 1 – COMPANY OVERVIEW AND BASIS OF PRESENTATION

PriceSmart, Inc.'s ("PriceSmart" or the "Company") business consists primarily of international membership shopping warehouse clubs similar to, but smaller in size than, warehouse clubs in the United States. As of May 31, 2012, the Company had 29 consolidated warehouse clubs in operation in 12 countries and one U.S. territory (five in Costa Rica, four each in Panama and Trinidad, three each in Guatemala and in the Dominican Republic, two each in El Salvador and Honduras and one each in Colombia, Aruba, Barbados, Jamaica, Nicaragua and the United States Virgin Islands), of which the Company owns 100% of the corresponding legal entities (see Note 2 - Summary of Significant Accounting Policies). The Company opened a new warehouse club in Santo Domingo, Dominican Republic ("Arroyo Hondo") on November 5, 2010 and a new membership warehouse club in Barranquilla, Colombia on August 19, 2011. The Company also acquired land in south Cali, Colombia on December 14, 2011 upon which it currently anticipates opening a new warehouse club in October 2012. Additionally, on January 9, 2012 the Company entered into an agreement to acquire property located in La Union, Cartago, Costa Rica, upon which the Company anticipates constructing its sixth membership warehouse club in Costa Rica with an anticipated opening in the summer of calendar year 2013. Finally, on March 15, 2012 the Company acquired land in north Cali, Colombia upon which it anticipates opening a new warehouse club in the spring of calendar year 2013. The initial warehouse sales and membership results experienced with the opening of the Barranquilla warehouse club has reinforced the Company's belief that Colombia could be a market for multiple PriceSmart warehouse clubs. The Company continues to explore other potential sites for future warehouse clubs in other major cities in Colombia as well as in its other markets.

Basis of Presentation - The interim consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q for interim financial reporting pursuant to the rules and regulations of the U.S. Securities and Exchange Commission ("SEC"). These interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the Company's Amendment No. 1 to Annual Report on Form 10-K/A for the fiscal year ended August 31, 2011 (the "2011 Form 10-K"). The interim consolidated financial statements include the accounts of PriceSmart, Inc., a Delaware corporation, and its subsidiaries. Inter-company transactions between the Company and its subsidiaries have been eliminated in consolidation.

In accordance with the Financial Accounting Standards Board's ("FASB") revised guidance establishing general accounting standards and disclosure of subsequent events, the Company has evaluated subsequent events through the date and time these financial statements were issued.

During fiscal year 2007 and during the first quarter of fiscal year 2012, the Company merged in each period a wholly owned subsidiary formed to purchase, develop and serve as a holding company for the land and buildings used by certain operating warehouse clubs (each, a "Landco") with one of the wholly owned subsidiaries formed to operate these warehouse clubs (each, an "Opco"). Each of the Landco entities involved in these mergers had a functional and reporting currency in U.S. dollars, and each of the related Opco entities that they were merged into had a foreign currency as a functional currency and U.S. dollars as a reporting currency. In each of these mergers, the Opco was the surviving entity, with the assets, liabilities and equity accounts of the Landco being transferred to the Opco and the Landco subsidiary ceasing to exist. Since the Landco entity ceased to exist, and all relevant economic activities previously performed by the Landco no longer exist, a significant change in economic facts and circumstances has been determined to have taken place, indicating that the functional currency has changed as the assets were transferred to the Opco. Upon this transfer, the Company is required to remeasure the non-monetary balance sheet items at historical exchange rates in order to produce the same result in terms of the functional currency that would have occurred if those items had been initially recorded in the foreign functional currency. As a result of the 2012 merger, and the resulting translation adjustments, the Company recorded in the first quarter of fiscal year 2012 a charge to comprehensive income for approximately $5.6 million relating to the fiscal year 2012 merger, with a corresponding reduction to Property and equipment, net for the same amount.

During the first quarter of fiscal year 2012, the Company identified errors in the consolidated financial statements for the fiscal year ended August 31, 2011 and for fiscal years previous to 2009. The errors relate to incorrect (i) accounting for the 2007 merger described above which impacted the translation of Property and equipment, net from foreign currencies to U.S. dollars and the related offset to Accumulated other comprehensive loss; and (ii) the translation of Property and equipment, net from foreign currencies to U.S. dollars and the related offset to Accumulated other comprehensive loss. The correction of these errors would have decreased comprehensive income by $6.4 million and increased comprehensive income by $3.1 million in fiscal year 2007 and 2011, respectively. The total of these corrections, which was recorded in the first quarter of fiscal 2012 as a charge to

PRICESMART, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

comprehensive income was approximately $3.3 million and decreased Property and equipment, net and increased Accumulated other comprehensive loss by the same amount.

The Company has analyzed the impact of these items and concluded that neither error would be material to any individual period, taking into account the requirements of the Securities and Exchange Commission ("SEC") Staff Accounting Bulletin No. 108, Considering the Effects of Prior Year Misstatements in the Current Year Financial Statements ("SAB 108"). In accordance with the relevant guidance, management evaluated the materiality of errors from a quantitative and qualitative perspective. Based on such evaluation, the Company concluded that correcting the cumulative errors, which decreased comprehensive income by approximately $3.3 million for the three month period ended November 30, 2011, would be immaterial to the expected full year results for fiscal 2012 and financial position as presented on the consolidated balance sheet. Correcting the error would not have had a material impact on any individual prior period presented in the 2011 Form 10-K or affect the trend of financial results. As provided by SAB 108, the error correction did not require the restatement of the consolidated financial statements for prior periods.

As a result of recording (i) the fiscal year 2012 merger and the resulting translation adjustment, (ii) the correction of the accounting for the 2007 merger, and (iii) the correction of an error in translation of Property and equipment, net from foreign currencies to U.S. dollars, the Company recorded an increase to Accumulated other comprehensive loss for $8.9 million within the first quarter of fiscal year 2012.

Monetary assets and liabilities in currencies other than the functional currency of the respective entity are revalued to the functional currency using the exchange rate on the balance sheet date. These foreign exchange transaction gains (losses), including repatriation of funds, have been reclassified from Cost of goods sold to Other income (expense) in the Consolidated Statements of Income for the fiscal year and interim periods reported for 2011. The Company's management believes that these foreign currency transactions are not directly matched to the recognition of cost of goods sold but are more closely linked to financing activities of the Company. These activities include the use of the extension of U.S dollar payables as a funding tool to meet the Company's subsidiary cash requirements and direct bank financing for U.S. dollar loans that constitute financing vehicles for expansion or development of subsidiaries, where once the cash is deposited into that subsidiary, it is fungible and can be used for any cash requirement of the entity such as capital, inter-company payments, working capital requirements, dividend payments and increases in restricted cash balances to comply with financing requirements. The Company believes that these reclassifications will allow for better comparability to other comparable companies with similar business models. The following table summarizes the amounts reclassified to conform with fiscal year 2012 presentation (in thousands):

	Three Months Ended				
	November 30, 2010	February 28, 2011	May 31, 2011	August 31, 2011	Total fiscal year 2011
Other income (expense) – (net previously reported)[1]	$(46)	$(260)	$1,838	$8	$1,540
Foreign exchange transaction gains reclassified from Cost of goods sold to Other income (expenses), net	378	454	529	963	2,324
Other income (expense), net – (currently reported)[2]	$332	$194	$2,367	$971	$3,864

	Three Months Ended				
	November 30, 2010	February 28, 2011	May 31, 2011	August 31, 2011	Total fiscal year 2011

(1)

Composition of beginning balance					
Other income (expense) –					
(previously reported):					
Gain/(loss) on sale	(53)	(176)	1,179	(187)	763
Currency gain/(loss)	7	(84)	659	195	