

EXPEDITORS INTERNATIONAL OF WASHINGTON INC
Form 10-Q
August 08, 2008

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 June 30, 2007

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: 0-13468

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.

(Exact name of registrant as specified in its charter)

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Washington
(State or other jurisdiction of
incorporation or organization)

91-1069248
(IRS Employer Identification Number)

1015 Third Avenue, 12th Floor, Seattle, Washington
(Address of principal executive offices)

98104
(Zip Code)

(206) 674-3400

(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 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

Accelerated filer

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

Smaller reporting company

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

At August 4, 2008, the number of shares outstanding of the issuer's Common Stock was 213,054,998.

PART I. FINANCIAL INFORMATION**Item 1. Financial Statements**EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.
AND SUBSIDIARIESCondensed Consolidated Balance Sheets
(In thousands, except share data)

(Unaudited)

	June 30, 2008	December 31, 2007
Assets		
Current assets:		
Cash and cash equivalents	\$ 703,488	\$ 574,599
Short-term investments	410	674
Accounts receivable, less allowance for doubtful accounts of \$13,822 at June 30, 2008 and \$14,830 at December 31, 2007	982,725	933,519
Deferred Federal and state income taxes	7,885	8,278
Other	53,456	17,627
Total current assets	1,747,964	1,534,697
Property and equipment, less accumulated depreciation and amortization of \$231,503 at June 30, 2008 and \$214,223 at December 31, 2007	505,263	497,892
Goodwill, net	7,927	7,927
Other intangibles, net	7,216	7,832
Other assets, net	21,334	20,717
	\$ 2,289,704	\$ 2,069,065
Liabilities and Shareholders Equity		
Current liabilities:		
Accounts payable	682,409	613,108
Accrued expenses, primarily salaries and related costs	158,427	129,669
Federal, state and foreign income taxes	31,343	26,976
Total current liabilities	872,179	769,753
Deferred Federal and state income taxes	76,923	55,533
Minority interest	18,050	17,208
Shareholders equity:		
Preferred stock, par value \$.01 per share		
Authorized 2,000,000 shares; none issued		

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Common stock, par value \$.01 per share

Authorized 320,000,000 shares; issued and outstanding 212,995,326 shares at June 30, 2008,
and 212,996,776 shares at December 31, 2007

	2,130	2,130
Additional paid-in capital	32,567	50,006
Retained earnings	1,247,023	1,143,464
Accumulated other comprehensive income	40,832	30,971
Total shareholders' equity	1,322,552	1,226,571
Commitments and contingencies		
	\$ 2,289,704	\$ 2,069,065

See accompanying notes to condensed consolidated financial statements.

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.
AND SUBSIDIARIESCondensed Consolidated Statements of Earnings
(In thousands, except share data)

(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2008	2007	2008	2007
Revenues:				
Airfreight	\$ 658,882	\$ 564,471	\$ 1,258,645	\$ 1,081,676
Ocean freight and ocean services	516,473	450,431	963,265	825,633
Customs brokerage and other services	278,900	243,716	539,666	470,255
Total revenues	1,454,255	1,258,618	2,761,576	2,377,564
Operating expenses:				
Airfreight consolidation	517,683	437,446	978,782	827,090
Ocean freight consolidation	419,767	364,917	780,207	663,808
Customs brokerage and other services	119,480	101,681	230,934	197,956
Salaries and related costs	215,535	197,393	421,350	380,154
Rent and occupancy costs	19,374	15,744	38,809	32,411
Depreciation and amortization	10,056	10,275	19,828	19,850
Selling and promotion	9,744	9,581	19,248	18,677
Other	29,645	19,843	53,883	41,355
Total operating expenses	1,341,284	1,156,880	2,543,041	2,181,301
Operating income	112,971	101,738	218,535	196,263
Interest expense	(75)	118	(146)	104
Interest income	4,915	5,531	9,879	10,750
Other, net	(162)	1,675	1,112	2,430
Other income, net	4,678	7,324	10,845	13,284
Earnings before income taxes and minority interest	117,649	109,062	229,380	209,547
Income tax expense	46,043	43,315	91,253	84,475
Net earnings before minority interest	71,606	65,747	138,127	125,072
Minority interest	(357)	(258)	(406)	(295)
Net earnings	\$ 71,249	\$ 65,489	\$ 137,721	\$ 124,777
Diluted earnings per share	\$.32	\$.30	\$.62	\$.56
Basic earnings per share	\$.33	\$.31	\$.65	\$.58

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Dividends declared and paid per common share	\$.16	\$.14	\$.16	\$.14
Weighted average diluted shares outstanding		220,515,987		221,716,414		220,490,452		222,283,372
Weighted average basic shares outstanding		213,275,229		213,251,710		213,168,730		213,339,478

See accompanying notes to condensed consolidated financial statements.

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.
AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows
(In thousands)

(Unaudited)

	Three months ended		Six months ended	
	2008	June 30, 2007	2008	June 30, 2007
Operating activities:				
Net earnings	\$ 71,249	\$ 65,489	\$ 137,721	\$ 124,777
Adjustments to reconcile net earnings to net cash provided by operating activities:				
Provision for losses on accounts receivable	(396)	(869)	(573)	(355)
Deferred income tax expense	7,647	6,772	16,473	12,240
Excess tax benefits from stock plans	(7,889)	(5,291)	(9,395)	(21,623)
Stock compensation expense	11,323	12,043	22,603	23,503
Depreciation and amortization	10,056	10,275	19,828	19,850
Gain on sale of property and equipment	(30)	(79)	(605)	(202)
Minority interest in earnings of consolidated entities	357	258	406	295
Other	515	354	932	688
Changes in operating assets and liabilities:				
Increase in accounts receivable	(91,778)	(70,962)	(32,024)	(13,261)
Decrease (increase) in other current assets	622	173	677	(504)
Increase in accounts payable and other current liabilities	67,024	76,080	82,102	62,445
Decrease in income taxes payable, net	(32,697)	(7,311)	(23,437)	(4,842)
Net cash provided by operating activities	36,003	86,932	214,708	203,011
Investing activities:				
Decrease in short-term investments	169	76	216	162
Purchase of property and equipment	(14,316)	(12,904)	(24,526)	(26,342)
Proceeds from sale of property and equipment	139	119	181	498
Prepayment on long-term land lease		(2,848)		(2,848)
Deposit on building purchase		(5,056)		(5,056)
Other	(308)	(1,188)	55	(1,528)
Net cash used in investing activities	(14,316)	(21,801)	(24,074)	(35,114)
Financing activities:				
Net distributions to minority interests		(316)	(107)	(316)
(Repayments) borrowings of short-term debt, net	(810)	(17)		203
Proceeds from issuance of common stock	15,537	12,602	20,151	27,868
Repurchases of common stock	(50,970)	(56,597)	(69,588)	(128,995)
Excess tax benefits from stock plans	7,889	5,291	9,395	21,623
Dividends paid	(34,163)	(29,902)	(34,163)	(29,902)
Net cash used in financing activities	(62,517)	(68,939)	(74,312)	(109,519)

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Effect of exchange rate changes on cash	3,352	2,034	12,567	5,306
(Decrease) increase in cash and cash equivalents	(37,478)	(1,774)	128,889	63,684
Cash and cash equivalents at beginning of period	740,966	576,816	574,599	511,358
Cash and cash equivalents at end of period	\$ 703,488	\$ 575,042	\$ 703,488	\$ 575,042
Interest and taxes paid:				
Interest	\$ 75	\$ 127	\$ 146	\$ 138
Income taxes	67,613	41,279	91,885	74,312

See accompanying notes to condensed consolidated financial statements.

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

Note 1. Summary of Significant Accounting Policies

The attached condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. As a result, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted. The Company believes that the disclosures made are adequate to make the information presented not misleading. The condensed consolidated financial statements reflect all adjustments, consisting of normal recurring items, which are, in the opinion of management, necessary to a fair statement of the results for the interim periods presented. These condensed consolidated financial statements should be read in conjunction with the financial statements and related notes included in the Company's Form 10-K as filed with the Securities and Exchange Commission on or about February 29, 2008.

Note 2. Comprehensive Income

Comprehensive income consists of net income and other gains and losses affecting shareholders' equity that, under generally accepted accounting principles in the United States, are excluded from net income. For the Company, these consist of foreign currency translation gains and losses and unrealized gains and losses on securities, net of related income tax effects.

The components of total comprehensive income for interim periods are presented in the following table:

(in thousands)	Three months ended June 30,		Six months ended June 30,	
	2008	2007	2008	2007
Net earnings	\$ 71,249	\$ 65,489	\$ 137,721	\$ 124,777
Foreign currency translation adjustments net of tax of \$(1,010) and \$(2,425) for the 3 months ended June 30, 2008 and 2007, and \$(5,310) and \$(3,315) for the 6 months ended June 30, 2008 and 2007.	1,875	4,504	9,861	6,156
Unrealized gain (loss) on securities net of tax of \$0 and \$(12) for the 3 months ended June 30, 2008 and 2007, and \$0 and \$1 for the 6 months ended June 30, 2008 and 2007.		18		(1)
Total comprehensive income	\$ 73,124	\$ 70,011	\$ 147,582	\$ 130,932

Note 3. Business Segment Information

The Company is organized functionally in geographic operating segments. Accordingly, management focuses its attention on revenues, net revenues, operating income, identifiable assets, capital expenditures, depreciation and amortization and equity generated in each of these geographical areas when evaluating the effectiveness of geographic management. The Company charges its subsidiaries and affiliates for services rendered in the United States on a cost recovery basis. Transactions among the Company's various offices are conducted using the same arms-length pricing methodologies the Company uses when its offices transact business with independent agents.

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Financial information regarding the Company's operations by geographic area for the three and six-months ended June 30, 2008 and 2007 are as follows:

(in thousands)	UNITED STATES	OTHER NORTH AMERICA	ASIA	EUROPE	AUSTRAL-ASIA	LATIN AMERICA	MIDDLE EAST	ELIMI-NATIONS	CONSOLI-DATED
Three months ended June 30, 2008:									
Revenues from unaffiliated customers	\$ 320,278	41,397	768,086	209,297	23,407	24,626	67,164		1,454,255
Transfers between geographic areas	26,842	2,623	5,629	11,257	2,158	3,649	4,539	(56,697)	
Total revenues	\$ 347,120	44,020	773,715	220,554	25,565	28,275	71,703	(56,697)	1,454,255
Net revenues	\$ 153,846	18,009	104,688	72,286	13,125	14,159	21,212		397,325
Operating income	\$ 33,469	3,272	47,543	15,779	4,117	3,553	5,238		112,971
Identifiable assets at quarter end	\$ 1,004,374	75,321	501,944	485,926	41,521	60,909	111,532	8,177	2,289,704
Capital expenditures	\$ 7,159	855	3,207	1,684	159	505	747		14,316
Depreciation and amortization	\$ 5,424	328	1,499	1,681	247	322	555		10,056
Equity	\$ 1,462,274	37,101	399,486	185,411	26,884	30,550	56,451	(875,605)	1,322,552
Three months ended June 30, 2007:									
Revenues from unaffiliated customers	\$ 260,796	32,765	710,104	162,100	17,057	19,377	56,419		1,258,618
Transfers between geographic areas	25,856	1,989	4,470	8,172	1,853	3,078	3,340	(48,758)	
Total revenues	\$ 286,652	34,754	714,574	170,272	18,910	22,455	59,759	(48,758)	1,258,618
Net revenues	\$ 143,206	15,377	100,479	58,600	9,812	10,950	16,150		354,574
Operating income	\$ 31,459	2,941	46,587	11,951	2,658	2,354	3,788		101,738
Identifiable assets at quarter end	\$ 893,335	69,599	431,106	395,022	30,617	37,310	82,642	(2,370)	1,937,261
Capital expenditures	\$ 7,843	688	1,188	2,141	198	267	579		12,904
Depreciation and amortization	\$ 5,304	331	1,222	2,393	225	417	383		10,275
Equity	\$ 1,256,503	32,692	326,036	134,925	20,114	19,571	39,555	(714,363)	1,115,033
Six months ended June 30, 2008:									
Revenues from unaffiliated customers	\$ 618,224	76,466	1,447,936	394,861	43,246	46,486	134,357		2,761,576
Transfers between geographic areas	50,923	4,696	10,740	21,759	4,292	6,956	8,536	(107,902)	
Total revenues	\$ 669,147	81,162	1,458,676	416,620	47,538	53,442	142,893	(107,902)	2,761,576
Net revenues	\$ 302,901	34,683	203,429	138,059	24,824	26,804	40,953		771,653
Operating income	\$ 66,013	6,399	93,573	28,220	7,589	6,819	9,922		218,535

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Identifiable assets at quarter end	\$	1,004,374	75,321	501,944	485,926	41,521	60,909	111,532	8,177	2,289,704
Capital expenditures	\$	10,795	1,191	6,510	3,294	353	776	1,607		24,526
Depreciation and amortization	\$	10,770	640	2,753	3,449	496	637	1,083		19,828
Equity	\$	1,462,274	37,101	399,486	185,411	26,884	30,550	56,451	(875,605)	1,322,552

**Six months ended
June 30, 2007:**

Revenues from unaffiliated customers	\$	506,521	60,851	1,312,135	318,479	31,840	38,748	108,990		2,377,564
Transfers between geographic areas		48,354	3,967	8,450	15,933	3,550	5,584	6,763	(92,601)	
Total revenues	\$	554,875	64,818	1,320,585	334,412	35,390	44,332	115,753	(92,601)	2,377,564
Net revenues	\$	278,673	30,077	193,632	114,627	18,739	20,745	32,217		688,710
Operating income	\$	59,522	5,670	91,471	22,102	5,062	4,406	8,030		196,263
Identifiable assets at quarter end	\$	893,335	69,599	431,106	395,022	30,617	37,310	82,642	(2,370)	1,937,261
Capital expenditures	\$	16,548	1,012	2,521	3,526	892	762	1,081		26,342
Depreciation and amortization	\$	10,473	662	2,597	4,130	425	817	746		19,850
Equity	\$	1,256,503	32,692	326,036	134,925	20,114	19,571	39,555	(714,363)	1,115,033

Note 4. Basic and Diluted Earnings per Share

The following table reconciles the numerator and the denominator of the basic and diluted per share computations for earnings per share for the three months and six months ended June 30, 2008 and 2007:

(Amounts in thousands, except share and per share amounts)	Three months ended June 30,		
	Net Earnings	Weighted Average Shares	Earnings Per Share
2008			
Basic earnings per share	\$ 71,249	213,275,229	\$.33
Effect of dilutive potential common shares		7,240,758	
Diluted earnings per share	\$ 71,249	220,515,987	\$.32
2007			
Basic earnings per share	\$ 65,489	213,251,710	\$.31
Effect of dilutive potential common shares		8,464,704	
Diluted earnings per share	\$ 65,489	221,716,414	\$.30

(Amounts in thousands, except share and per share amounts)	Six months ended June 30,		
	Net Earnings	Weighted Average Shares	Earnings Per Share
2008			
Basic earnings per share	\$ 137,721	213,168,730	\$.65
Effect of dilutive potential common shares		7,321,722	
Diluted earnings per share	\$ 137,721	220,490,452	\$.62
2007			
Basic earnings per share	\$ 124,777	213,339,478	\$.58
Effect of dilutive potential common shares		8,943,894	
Diluted earnings per share	\$ 124,777	222,283,372	\$.56

The following shares have been excluded from the computation of diluted earnings per share because the effect would have been antidilutive:

	Three months ended June 30,		Six months ended June 30,	
	2008	2007	2008	2007
Shares	6,730,280	4,852,570	6,730,280	3,035,010

Note 5. Stock and Cash Dividends

On May 8, 2008, the Board of Directors declared a semi-annual cash dividend of \$.16 per share payable on June 16, 2008 to shareholders of record as of June 2, 2008. The dividend of \$34 million was paid on June 16, 2008.

On May 3, 2007, the Board of Directors declared a semi-annual cash dividend of \$.14 per share payable on June 15, 2007 to shareholders of record as of June 1, 2007. The dividend of \$30 million was paid on June 15, 2007.

Note 6. Shareholders' Equity

A. Share-Based Compensation Plans

The Company provides compensation benefits by granting stock options and employee stock purchase rights to its employees and restricted stock to its directors.

In May 2008, the shareholders approved the Company's 2008 Plan, which made available a total of 3,000,000 shares of the Company's common stock for purchase upon exercise of options granted under the 2008 Plan. The Company's annual grant of option awards generally takes place during the second quarter of each fiscal year. For the six-month periods ended June 30, 2008 and 2007, 2,080,315 and 1,930,510 options were granted, respectively. The grant of employee stock purchase rights and the issuance of shares under the employee stock purchase plan are generally made in the third quarter of each fiscal year and none were issued in the three and six-month periods ended June 30, 2008 and 2007.

In May 2008, the shareholders approved the Company's 2008 Directors' restricted stock plan (the 2008 Directors' Plan), which provides for annual awards of restricted stock to non-employee directors and is intended to replace the 1993 Directors' Non-qualified Stock Option Plan. The shareholder approval made available for grant 200,000 shares of the Company's common stock. The plan provides for an annual grant of restricted stock awards with a fair market value equal to \$200,000 to each participant. Each restricted stock award under the 2008 Directors' Plan vests in equal amounts monthly over one year. Restricted shares entitle the grantees to all shareholder rights once vested, except for cash dividends and transfer rights which are forfeited until the final vesting date of the award. If a participant's service as director is terminated, any unvested portion of an award will be forfeited unless the Compensation Committee of the Board of Directors determines otherwise.

B. Share-Based Compensation Expense

The Company recognizes stock compensation expense on a straight-line basis over the period the stock awards become vested.

The Company recognizes compensation expense based on the estimated fair value of options awarded under its fixed stock option and employee stock purchase rights plans. The fair value of each option grant was estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions used for grants issued during the six months ended June 30, 2008 and 2007.

	Six months ended June 30,			
	2008		2007	
Dividend yield	.72%		.65%	
Volatility	34	37%	35	41%
Risk-free interest rates	3.46%		4.69	4.75%
Expected life (years) - stock option plans	6.50	7.99	6.54	8.70
Weighted average fair value of stock options granted during the period	\$	17.85	\$	18.49

The compensation expense for restricted stock awards is based on the fair market value of the Company's shares of common stock on the date of grant. On June 1, 2008, 25,488 restricted shares were granted with a fair value of \$47.08 per share.

Total stock compensation expense and the total related tax benefit recognized in the three and six-months ended June 30, 2008 and 2007 are as follows:

	Three months ended June 30,		Six months ended June 30,	
	2008	2007	2008	2007
Stock compensation expense	\$ 11,323	\$ 12,043	\$ 22,603	\$ 23,503
Recognized tax benefit	\$ 228	\$ 482	\$ 591	\$ 1,070

Note 7. Income Taxes

Based on management's review of the Company's tax positions the Company had no significant unrecognized tax benefits as of June 30, 2008 and December 31, 2007.

The Company or one of its subsidiaries files income tax returns in the U.S. federal jurisdiction and various state, local and foreign jurisdictions. The Company is no longer subject to U.S. federal income tax examinations by tax authorities for years prior to 2004. In October 2007, the Internal Revenue Service initiated an audit of the Company's federal income tax return for the year 2005. With respect to state and local jurisdictions and countries outside of the United States, with limited exceptions, the Company and its subsidiaries are no longer subject to income tax audits for years prior to 2000. In the normal course of business, the Company is subject to examination by taxing authorities throughout the world. Although the outcome of tax audits is always uncertain, the Company believes that adequate amounts of tax, interest and penalties have been provided for any adjustments that may result from these open tax years.

The Company recognizes interest expense related to unrecognized tax benefits or underpayment of income taxes in interest expense and recognizes penalties in operating expenses. Any interest and penalties expensed in relation to the underpayment of income taxes were insignificant for the three and six months ended June 30, 2008 and 2007.

Note 8. Recent Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 157, Fair Value Measurements (SFAS 157), supplemented by FASB Financial Staff Position 157-1 and 2. SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements, the FASB having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, this Statement does not require any new fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company adopted the provisions of SFAS 157 beginning in the first quarter of 2008, except for certain nonfinancial assets and liabilities for which it will adopt the provisions of SFAS 157 in the first quarter of 2009. The adoption of SFAS 157 had no material impact on the Company's consolidated financial condition or results of operations.

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In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS 159). Under the provisions of SFAS 159, companies may choose to account for eligible financial instruments, warranties and insurance contracts at fair value on a contract-by-contract basis. Changes in fair value will be recognized in earnings each reporting period. SFAS 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company adopted the provisions of SFAS 159 beginning in the first quarter of 2008. The adoption of SFAS 159 had no material impact on the Company's consolidated financial condition or results of operations.

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 changes the accounting and reporting for minority interests, whi