

Houston Wire & Cable CO
Form 10-Q
November 08, 2016

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
X ACT OF 1934**

For the quarterly period ended September 30, 2016

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: 000-52046

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

36-4151663

(I.R.S. Employer Identification No.)

10201 North Loop East

Houston, Texas

(Address of principal executive offices)

77029

(Zip Code)

(713) 609-2100

(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 or a smaller reporting company. See definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act

Large Accelerated Filer ☐ Accelerated Filer ☒ 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 ☒

At November 1, 2016 there were 16,380,704 outstanding shares of the registrant's common stock, \$0.001 par value per share.

HOUSTON WIRE & CABLE COMPANY

Form 10-Q

For the Quarter Ended September 30, 2016

INDEX

PART I. FINANCIAL INFORMATION

Item 1.	Financial Statements (Unaudited)	
	<u>Consolidated Balance Sheets</u>	2
	<u>Consolidated Statements of Operations</u>	3
	<u>Consolidated Statements of Cash Flows</u>	4
	<u>Notes to Consolidated Financial Statements</u>	5
Item 2.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	9
	<u>Overview</u>	9
	<u>Cautionary Statement for Purposes of the "Safe Harbor"</u>	9
	<u>Results of Operations</u>	10
	<u>Impact of Inflation and Commodity Prices</u>	13
	<u>Liquidity and Capital Resources</u>	13
	<u>Contractual Obligations</u>	14
Item 3.	<u>Quantitative and Qualitative Disclosures about Market Risk</u>	14
Item 4.	<u>Controls and Procedures</u>	14

PART II. OTHER INFORMATION 14

Item 1.	<u>Legal Proceedings</u>	14
Item 1A.	<u>Risk Factors</u>	14
Item 2.	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	15
Item 3.	<u>Defaults Upon Senior Securities</u>	15
Item 4.	<u>Mine Safety Disclosures</u>	15
Item 5.	<u>Other Information</u>	15
Item 6.	<u>Exhibits</u>	16

	<u>Signature Page</u>	17
--	-----------------------	----

HOUSTON WIRE & CABLE COMPANY**Consolidated Balance Sheets**

(In thousands, except share data)

	September 30, 2016 (unaudited)	December 31, 2015
Assets		
Current assets:		
Accounts receivable, net	\$ 42,929	\$ 46,250
Inventories, net	63,563	75,777
Income taxes	1,577	932
Prepays	1,095	648
Total current assets	109,164	123,607
Property and equipment, net	10,884	10,899
Intangible assets, net	4,734	5,984
Goodwill	12,504	14,866
Deferred income taxes	4,090	3,338
Other assets	415	419
Total assets	\$ 141,791	\$ 159,113
Liabilities and stockholders' equity		
Current liabilities:		
Book overdraft	\$ 1,102	\$ 3,701
Trade accounts payable	8,488	6,380
Accrued and other current liabilities	11,053	9,568
Total current liabilities	20,643	19,649
Debt	28,619	39,188
Other long term obligations	516	275
Total liabilities	49,778	59,112
Stockholders' equity:		
Preferred stock, \$0.001 par value; 5,000,000 shares authorized, none issued and outstanding	—	—
Common stock, \$0.001 par value; 100,000,000 shares authorized: 20,988,952 shares issued: 16,402,204 and 16,712,626 outstanding at September 30, 2016 and December 31, 2015, respectively	21	21
Additional paid-in-capital	55,007	54,621
Retained earnings	99,374	106,048
Treasury stock	(62,389)	(60,689)
Total stockholders' equity	92,013	100,001

Edgar Filing: Houston Wire & Cable CO - Form 10-Q

Total liabilities and stockholders' equity	\$ 141,791	\$ 159,113
--	------------	------------

The accompanying Notes are an integral part of these Consolidated Financial Statements.

HOUSTON WIRE & CABLE COMPANY**Consolidated Statements of Operations**

(Unaudited)

(In thousands, except share and per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Sales	\$65,222	\$78,260	\$192,387	\$237,819
Cost of sales	53,177	62,129	154,513	187,029
Gross profit	12,045	16,131	37,874	50,790
Operating expenses:				
Salaries and commissions	7,148	7,311	20,895	21,717
Other operating expenses	5,969	6,300	17,302	18,629
Depreciation and amortization	732	737	2,198	2,175
Impairment charge	—	—	2,384	2,994
Total operating expenses	13,849	14,348	42,779	45,515
Operating income (loss)	(1,804)	1,783	(4,905)	5,275
Interest expense	129	237	453	719
Income (loss) before income taxes	(1,933)	1,546	(5,358)	4,556
Income tax expense (benefit)	(494)	870	(1,178)	2,313
Net income (loss)	\$(1,439)	\$676	\$(4,180)	\$2,243
Earnings (loss) per share:				
Basic	\$(0.09)	\$0.04	\$(0.26)	\$0.13
Diluted	\$(0.09)	\$0.04	\$(0.26)	\$0.13
Weighted average common shares outstanding:				
Basic	16,302,870	17,017,334	16,388,892	17,137,730
Diluted	16,302,870	17,072,128	16,388,892	17,190,664
Dividend declared per share	\$0.03	\$0.12	\$0.15	\$0.36

The accompanying Notes are an integral part of these Consolidated Financial Statements.

HOUSTON WIRE & CABLE COMPANY**Consolidated Statements of Cash Flows**

(Unaudited)

(In thousands)

	Nine Months Ended September 30,	
	2016	2015
Operating activities		
Net income (loss)	\$(4,180)	\$2,243
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Impairment charge	2,384	2,994
Depreciation and amortization	2,198	2,175
Amortization of unearned stock compensation	626	668
Provision for inventory obsolescence	355	351
Deferred income taxes	(752)	(727)
Other non-cash items	(11)	70
Changes in operating assets and liabilities:		
Accounts receivable	3,360	10,370
Inventories	11,859	11,667
Book overdraft	(2,599)	(808)
Trade accounts payable	2,108	1,264
Accrued and other current liabilities	1,486	(278)
Income taxes	(645)	(909)
Other operating activities	(230)	(288)
Net cash provided by operating activities	15,959	28,792
Investing activities		
Expenditures for property and equipment	(955)	(2,946)
Net cash used in investing activities	(955)	(2,946)
Financing activities		
Borrowings on revolver	195,914	233,187
Payments on revolver	(206,483)	(248,208)
Payment of dividends	(2,477)	(6,166)
Purchase of treasury stock	(1,958)	(4,659)
Net cash used in financing activities	(15,004)	(25,846)
Net change in cash	—	—
Cash at beginning of period	—	—

Cash at end of period	\$—	\$—
-----------------------	-----	-----

The accompanying Notes are an integral part of these Consolidated Financial Statements.

HOUSTON WIRE & CABLE COMPANY
Notes to Consolidated Financial Statements

(Unaudited)

1. Basis of Presentation and Principles of Consolidation

Houston Wire & Cable Company (the “Company”), through its wholly owned subsidiaries, provides wire and cable, hardware and related services to the U.S. market through eighteen locations in thirteen states throughout the United States as of September 30, 2016. The Company has no other business activity.

The consolidated financial statements as of September 30, 2016 and for the nine months ended September 30, 2016 and 2015 have been prepared following accounting principles generally accepted in the United States (“GAAP”) for interim financial information and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, considered necessary for a fair presentation of the results of these interim periods have been included. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for the full year. All significant inter-company balances and transactions have been eliminated. The Company has evaluated subsequent events through the time these financial statements in this Form 10-Q were filed with the Securities and Exchange Commission (the “SEC”).

The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. The most significant estimates are those relating to the inventory obsolescence reserve, the reserve for returns and allowances, vendor rebates and asset impairments. Actual results could differ materially from the estimates and assumptions used for the preparation of the financial statements.

For further information, refer to the consolidated financial statements and footnotes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2015 filed with the SEC.

Recent Accounting Pronouncements

The Financial Accounting Standards Board (the “FASB”) Accounting Standards Codification (“ASC”) is the sole source of authoritative GAAP other than SEC issued rules and regulations that apply only to SEC registrants. The FASB

issues an Accounting Standard Update (“ASU”) to communicate changes to the codification. The Company considers the applicability and impact of all ASUs. The following recently issued ASUs are relevant to the Company.

In August 2016, the FASB issued ASU No. 2016-15, “Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments.” The amendments in this ASU address eight cash flow issues with the intention of reducing current diversity in practice among business entities. The Company will evaluate the eight issues in the amendment and determine if any changes are necessary for compliance. ASU 2016-15 is effective for annual and interim periods beginning after December 15, 2017; early adoption is permitted and should be applied retrospectively where practical. The Company will determine the date of adoption, once the Company has evaluated the impact of this ASU.

In March 2016, the FASB issued ASU No. 2016-09, “Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting.” The new guidance addresses several aspects of the accounting for share-based payment award transactions, including: (a) the recognition of the income tax effects of awards in the income statement when the awards vest, forfeit, or are settled, thus eliminating additional paid-in-capital pools, (b) classification of awards as either equity or liabilities, and (c) classification on the statement of cash flows. This update is effective for public companies for fiscal years beginning after December 15, 2016 with early adoption permitted. The Company is currently evaluating the elections the Company may make as well as the effects the adoption of this guidance may have on the Company's consolidated financial statements and will adopt this ASU in the first quarter of 2017.

In February 2016, the FASB issued ASU No. 2016-02, “Leases (Topic 842).” Under the new guidance, a lessee will be required to recognize assets and liabilities for leases greater than 1 year, regardless of whether they were previously accounted for as capital or operating leases. This update is effective for public companies for fiscal years beginning after December 15, 2018 with early adoption permitted. The Company is currently evaluating the impacts of adopting as well as the timing of when it will adopt this ASU.

In November 2015, the FASB issued ASU No. 2015-17, “Income Taxes (Topic 740) — Balance Sheet Classification of Deferred Taxes.” ASU No. 2015-17 eliminates the requirement to classify deferred tax assets and liabilities as current or long-term based on how the related assets or liabilities are classified. All deferred taxes are now required to be classified as long-term including any associated valuation allowances. This guidance is effective for public companies for fiscal years beginning after December 15, 2016 with early adoption permitted on either a prospective or retrospective basis. The Company adopted this guidance in the third quarter and has applied it retrospectively. It did not have a material impact on the consolidated financial statements.

In July 2015, the FASB issued ASU No. 2015-11, "Simplifying the Measurement of Inventory (Topic 330)," which changes guidance for subsequent measurement of inventory within the scope of the update from the lower of cost or market to the lower of cost and net realizable value. This update is effective for annual and interim periods beginning after December 15, 2016 and early adoption is permitted. The Company does not believe there will be any material impact upon the adoption of this guidance on the Company's consolidated financial statements and will adopt this ASU in the first quarter of 2017.

In April 2015, the FASB issued ASU No. 2015-03, "Simplifying the Presentation of Debt Issuance Costs (Subtopic 835-30)." The amendments in this ASU require debt issuance costs to be presented on the balance sheet as a direct reduction from the carrying amount of the related debt liability. However, the guidance in this ASU did not address the presentation or subsequent measurement of debt issuance costs related to line-of-credit arrangements. As a result, in August 2015 the FASB issued ASU No. 2015-15 "Interest—Imputation of Interest (Subtopic 835-30): Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Agreements," to clarify that, with respect to a line-of-credit agreement, the SEC staff would not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement. The Company adopted this guidance in the first quarter and will continue to treat debt issuance costs associated with its revolving credit facility as a deferred asset and amortize the deferred asset over the term of the credit agreement. Therefore, the adoption did not have any impact on the Company's financial position or results of operations.

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)," which supersedes the revenue recognition requirements in ASC Topic 605, "Revenue Recognition," and most industry-specific guidance. This ASU is based on the principle that revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments, and assets recognized from costs incurred to obtain or fulfill a contract. The amendments in the ASU must be applied using one of two retrospective methods and are effective for annual and interim periods beginning after December 15, 2017. Early adoption for annual and interim periods beginning after December 31, 2016 is permitted. The Company is still evaluating the impact of this ASU on its financial position and results of operations, timing of adoption, and which implementation method the Company will use.

2.Earnings (loss) per Share

Basic earnings (loss) per share are calculated by dividing net income (loss) by the weighted average number of common shares outstanding. Diluted earnings (loss) per share include the dilutive effects of stock options and unvested restricted stock awards and units.

Edgar Filing: Houston Wire & Cable CO - Form 10-Q

The following reconciles the denominator used in the calculation of diluted earnings (loss) per share:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2016	2015	2016	2015
Denominator:				
Weighted average common shares for basic earnings (loss) per share	16,302,870	17,017,334	16,388,892	17,137,730
Effect of dilutive securities	—	54,794	—	52,934
Weighted average common shares for diluted earnings (loss) per share	16,302,870	17,072,128	16,388,892	17,190,664

The weighted average common shares for diluted earnings (loss) per share exclude stock options and unvested restricted stock awards and units to purchase 736,968 and 632,736 shares for the three months ended September 30, 2016 and 2015, respectively, and 772,012 and 606,405 shares for the nine months ended September 30, 2016 and 2015. These securities have been excluded from the calculation, as including them would have an anti-dilutive effect on earnings (loss) per share for the respective periods.

3. Impairment of Goodwill and Intangibles

During the second quarter of 2016 and prior to the annual impairment test of goodwill in October, the Company concluded that impairment indicators existed at the Houston Wire & Cable (HWC) reporting unit, due to a decline in the overall financial performance, decrease in the market capitalization and overall market demand. In the second quarter, the Company also concluded that there were impairment indicators for certain of the Company's tradenames related to the Southwest Wire Rope (Southwest) and Southern Wire reporting units.

The Company performed step one of the impairment test and concluded that the fair value of the HWC reporting unit was less than its carrying value. Therefore, the Company performed step two of the impairment analysis. The step one test also indicated that one of the tradenames at Southern Wire was impaired, and the Company recorded a non-cash charge of less than \$0.1 million against the tradenames during the quarter ended June 30, 2016.

Step two of the impairment analysis measures the impairment charge by allocating the HWC reporting unit's fair value to all of the assets and liabilities of the reporting unit in a hypothetical analysis that calculates implied fair value of goodwill in the same manner as if the reporting unit was being acquired in a business combination and recording the deferred tax impact. Any excess of the carrying value of the reporting unit's goodwill over the implied fair value of the reporting unit's goodwill is recorded as an impairment loss.

The fair value of the HWC reporting unit was estimated using a discounted cash flow model (income approach) and a guideline public company method, giving 50% weight to each. The material assumptions used included a weighted average cost of capital of 11.0% and a long-term growth rate of 3-7% for the income approach and an adjusted invested capital multiple of 0.2 times revenue and a control premium of 10.0% for the guideline public company method. The carrying value of the HWC reporting unit's goodwill was \$2.4 million and its implied fair value resulting from step two of the impairment test was zero. As a result, the Company recorded a non-cash goodwill impairment charge of \$2.4 million during the quarter ended June 30, 2016.

The fair value for goodwill and tradenames (indefinite-lived intangible assets) were both determined using a Level 3 measurement approach. The Level 3 value of all of the Company's tradenames at June 30, 2016 was \$4.5 million.

During the second quarter of 2015 and prior to the annual impairment test of goodwill in October, the Company concluded that impairment indicators existed at the Southwest Wire Rope (Southwest) reporting unit, due to a decline in the overall financial performance and overall market demand. Impairment indicators also existed for certain of the Company's tradenames related to the Southwest and Southern Wire reporting units.

After performing the necessary analysis the Company recorded, during the quarter ended June 30, 2015, a non-cash charge of \$0.4 million against the tradenames and a non-cash goodwill impairment charge of \$2.6 million.

4. Debt

On October 1, 2015, HWC Wire & Cable Company, as borrower, entered into the Fourth Amended and Restated Loan and Security Agreement (the "2015 Loan Agreement"), with Bank of America, N.A., as agent and lender, and the Company, as guarantor, executed a Third Amended and Restated Guaranty of the borrower's obligations thereunder. The 2015 Loan Agreement provides a \$100 million revolving credit facility, bears interest at the agent's base rate, with a London Interbank Offered Rate ("LIBOR") rate option, and expires on September 30, 2020. Under certain circumstances, the Company may request an increase in the commitment by an additional \$50 million. The 2015 Loan Agreement is secured by substantially all of the property of the Company, other than real estate. Availability under the 2015 Loan Agreement is limited to a borrowing base equal to 85% of the value of eligible accounts receivable, plus the lesser of 70% of the value of eligible inventory or 90% of the net orderly liquidation value percentage of the value

of eligible inventory, in each case less certain reserves. The 2015 Loan Agreement was amended on October 3, 2016 in connection with the Vertex acquisition. See Note 8.

Portions of the loan may be converted to LIBOR loans in minimum amounts of \$1.0 million and integral multiples of \$0.1 million. LIBOR loans bear interest at the British Bankers Association LIBOR Rate plus 100 to 150 basis points based on availability, and loans not converted to LIBOR loans bear interest at a fluctuating rate equal to the greatest of the agent's prime rate, the federal funds rate plus 50 basis points, or 30-day LIBOR plus 150 basis points. The unused commitment fee is 25 basis points.

The 2015 Loan Agreement includes, among other things, covenants that require the Company to maintain a specified minimum fixed charge coverage ratio, unless certain availability levels exist. Additionally, the 2015 Loan Agreement allows for the unlimited payment of dividends and repurchases of stock, subject to the absence of events of default and maintenance of a fixed charge coverage ratio and minimum level of availability. The 2015 Loan Agreement contains certain provisions that may cause the debt to be classified as a current liability, in accordance with GAAP, if availability falls below certain thresholds, even though the ultimate maturity date under the loan agreement remains as September 30, 2020. At September 30, 2016, the Company was in compliance with the availability-based covenants governing its indebtedness.

The carrying amount of long term debt approximates fair value as it bears interest at variable rates. The fair value is a Level 2 measurement as defined in ASC Topic 820, "Fair Value Measurement."

5. Stockholders' Equity

During each of the first and second quarters of 2016, the Board of Directors approved a quarterly dividend of \$0.06 per share payable to stockholders and during the third quarter of 2016, the Board of Directors approved a quarterly dividend of \$0.03 per share payable to stockholders. Dividends paid were \$2.5 million and \$6.2 million during the nine months ended September 30, 2016 and 2015, respectively.

6. Stock Based Compensation

Stock Option Awards

There were no stock option awards granted during the first nine months of 2016 or 2015.

Restricted Stock Awards and Restricted Stock Units

Following the Annual Meeting of Stockholders on May 3, 2016, the Company awarded restricted stock units with a value of \$50,000 to each non-employee director who was elected or re-elected, for an aggregate of 35,515 restricted stock units. Each award of restricted stock units vests at the date of the 2017 Annual Meeting of Stockholders. Each non-employee director is entitled to receive a number of shares of the Company's common stock equal to the number of vested restricted stock units, together with dividend equivalents from the date of grant, at such time as the director's service on the board terminates for any reason.

On August 4, 2016, the Company granted 7,000 shares of restricted stock to a new member of the management team. These shares vest in one third increments, on the third, fourth and fifth anniversaries of the date of grant as long as the recipient is then employed by the Company. Any dividends declared will be accrued and paid to the recipient if and when the related shares vest.

Total stock-based compensation cost was \$0.2 million for each of the three months ended September 30, 2016 and 2015 and \$0.6 million and \$0.7 million for the nine months ended September 30, 2016 and 2015, respectively, and is included in salaries and commissions.

7. Commitments and Contingencies

As part of the acquisition of Southwest Wire and Southern Wire in 2010, the Company assumed the liability for the post-remediation monitoring of the water quality at one of the acquired facilities in Louisiana. The expected liability of \$0.1 million at September 30, 2016 relates to the cost of the monitoring, which the Company estimates will be incurred over approximately the next two years, and also the cost to plug the wells. Remediation work was completed prior to the acquisition in accordance with the requirements of the Louisiana Department of Environmental Quality.

The Company, along with many other defendants, has been named in a number of lawsuits in the state courts of Minnesota, North Dakota, and South Dakota alleging that certain wire and cable which may have contained asbestos caused injury to the plaintiffs who were exposed to this wire and cable. These lawsuits are individual personal injury suits that seek unspecified amounts of money damages as the sole remedy. It is not clear whether the alleged injuries occurred as a result of the wire and cable in question or whether the Company, in fact, distributed the wire and cable alleged to have caused any injuries. The Company maintains general liability insurance that, to date, has covered the defense of and all costs associated with these claims. In addition, the Company did not manufacture any of the wire and cable at issue, and the Company would rely on any warranties from the manufacturers of such cable if it were determined that any of the wire or cable that the Company distributed contained asbestos which caused injury to any of these plaintiffs. In connection with ALLTEL's sale of the Company in 1997, ALLTEL provided indemnities with respect to costs and damages associated with these claims that the Company believes it could enforce if its insurance coverage proves inadequate.

There are no legal proceedings pending against or involving the Company that, in management's opinion, based on the current known facts and circumstances, are expected to have a material adverse effect on the Company's consolidated financial position, cash flows, or results from operations.

8.Subsequent Events

On October 3, 2016, HWC Wire & Cable Company (the "Buyer"), a subsidiary of the Company acquired all of the issued and outstanding shares of common stock of Vertex Corporate Holdings, Inc. and its subsidiaries ("Vertex") from DXP Enterprises, Inc. ("DXP") pursuant to a Stock Purchase Agreement, dated as of October 3, 2016 between DXP and the Buyer (the "Purchase Agreement"). The Company has guaranteed the obligations of the Buyer under the Purchase Agreement. Vertex is engaged in the wholesale distribution of industrial fasteners.

The purchase price for the acquisition consisted of \$32.3 million in cash and is subject to a post-closing adjustment based on the net working capital of Vertex as of the closing date. The Buyer financed the payment of the purchase price through borrowings under an amendment to the 2015 Loan Agreement.

In addition, the Company granted 21,000 shares of restricted stock to four members of the Vertex management team. The shares will vest and declared dividends will be accrued, subject to their employment with the Company.

Also on October 3, 2016, in connection with the Vertex acquisition, the Buyer, the Company, Vertex, and Bank of America, N.A., as agent and lender, entered into a First Amendment to the Fourth Amended and Restated Loan and Security Agreement (the "Loan Agreement Amendment") amending the 2015 Loan Agreement. The Loan Agreement Amendment adds Vertex as borrower (and lien grantor) and provides the terms for inclusion of Vertex's eligible accounts receivable and eligible inventory in the borrowing base for the 2015 Loan Agreement. The 2015 Loan Agreement was expanded to include incremental availability on eligible accounts receivable and inventory up to \$5 million, which will be amortized quarterly, effective April 1, 2017, over two and a half years. Total borrowing capacity will remain at \$100 million.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following Management's Discussion and Analysis ("MD&A") is intended to help the reader understand the Company's financial position and results of operations. This MD&A is provided as a supplement to the Company's Consolidated Financial Statements (unaudited) and the accompanying Notes to Consolidated Financial Statements (unaudited) and should be read in conjunction with the MD&A included in the Company's Form 10-K for the year ended December 31, 2015.

Overview

We are one of the largest distributors of wire and cable and related services to the U.S. market. We provide our customers with a single-source solution for wire and cable, hardware and related services by offering a large selection of in-stock items, exceptional customer service and high levels of product expertise.

Critical Accounting Policies

The preparation of our consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets and liabilities, revenue and expenses. On an on-going basis, we make and evaluate estimates and judgments, including those related to the inventory obsolescence reserve, the reserve for returns and allowances, vendor rebates and asset impairments. We base our estimates on historical experience and various other assumptions that we believe are reasonable under the circumstances; the results of which form the basis for making judgments about amounts and timing of revenue and expenses, the carrying values of assets and the recorded amounts of liabilities that are not readily apparent from other sources. Actual results may differ from these estimates and such estimates may change if the underlying conditions or assumptions change. We have discussed the development and selection of critical accounting policies and estimates with the Audit Committee of our Board of Directors, and the Audit Committee has reviewed our related disclosures. The critical accounting policies related to the estimates and judgments are discussed in our Annual Report on Form 10-K for the year ended December 31, 2015 under Management's Discussion and Analysis of Financial Condition and Results of Operations. There have been no changes to our critical accounting policies and estimates during the nine months ended September 30, 2016.

Cautionary Statement for Purposes of the "Safe Harbor"

Forward-looking statements in this report are made in reliance upon the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements may relate to, but are not limited to, information or assumptions about our sales and marketing strategy, sales (including pricing), income, operating income or gross margin improvements, working capital, cash flow, interest rates, impact of changes in accounting standards, future economic performance, management's plans, goals and objectives for future operations, acquired businesses and growth or the assumptions relating to any of the forward-looking statements. These statements can be identified by the fact that they do not relate strictly to historical or current facts. They use words such as "aim", "anticipate", "believe", "could", "estimate", "expect", "intend", "may", "plan", "project", "should", "will be", "will continue", "would" and other words and terms of similar meaning in conjunction with a discussion of future operating or financial performance. The Company cautions that forward-looking statements are not guarantees because there are inherent difficulties in predicting future results. Actual results could differ materially from those expressed or implied in the forward-looking statements. The factors listed under "Risk Factors" in the Company's Annual Report on Form 10-K for the year ended December 31, 2015, as well as any cautionary language in this report, provide examples of risks, uncertainties and events that may cause our actual results to differ materially from the expectations we describe in our forward-looking statements.

Results of Operations

The following table shows, for the periods indicated, information derived from our consolidated statements of operations, expressed as a percentage of net sales for the periods presented.

	Three Months Ended September 30, 2016		2015		Nine Months Ended September 30, 2016		2015	
Sales	100.0	%	100.0	%	100.0	%	100.0	%
Cost of sales	81.5	%	79.4	%	80.3	%	78.6	%
Gross profit	18.5	%	20.6	%	19.7	%	21.4	%
Operating expenses:								
Salaries and commissions	11.0	%	9.3	%	10.9	%	9.1	%
Other operating expenses	9.2	%	8.1	%	9.0	%	7.8	%
Depreciation and amortization	1.1	%	0.9	%	1.1	%	0.9	%
Impairment charge	—		—		1.2	%	1.3	%
Total operating expenses	21.2	%	18.3	%	22.2	%	19.1	%
Operating income (loss)	(2.8	)%	2.3	%	(2.5	)%	2.2	%
Interest expense	0.2	%	0.3	%	0.2	%	0.3	%
Income (loss) before income taxes	(3.0	)%	2.0	%	(2.8	)%	1.9	%
Income tax expense (benefit)	(0.8	)%	1.1	%	(0.6	)%	1.0	%
Net income (loss)	(2.2	)%	0.9	%	(2.2	)%	0.9	%

Note: Due to rounding, percentages may not add up to total operating expenses, operating income (loss), income (loss) before income taxes or net income (loss).

Comparison of the Three Months Ended September 30, 2016 and 2015

Sales

Three Months Ended

Edgar Filing: Houston Wire & Cable CO - Form 10-Q

	September 30,		
(Dollars in millions)	2016	2015	Change
Sales	\$65.2	\$78.3	\$(13.0) (16.7)%

Our sales for the third quarter decreased 16.7% to \$65.2 million from \$78.3 million in 2015. We estimate that, when adjusted for the fluctuation in metal prices, sales for 2016 were down approximately 10% compared to the third quarter of 2015. Our project business, which targets end markets encompassing Environmental Compliance, Engineering & Construction, Industrials, Utility Power Generation, and Mechanical Wire Rope, is estimated to have decreased 52%, or approximately 45% on a metals adjusted basis, from 2015. Maintenance, Repair, and Operations (MRO) sales increased 1%, or approximately 8% when adjusted for metals, from 2015.

Gross Profit

	Three Months Ended		
	September 30,		
(Dollars in millions)	2016	2015	Change
Gross profit	\$12.0	\$16.1	\$(4.1) (25.3)%
Gross margin	18.5 %	20.6 %	(2.1)%

Gross profit decreased 25.3% to \$12.0 million in 2016 from \$16.1 million in 2015. The decrease in gross profit is primarily attributable to the lower sales in 2016. Gross margin (gross profit as a percent of sales) fell to 18.5% in 2016 from 20.6% in 2015, primarily due to competitive market conditions.

Operating Expenses

(Dollars in millions)	Three Months Ended			
	September 30,			
	2016	2015	Change	
Operating expenses:				
Salaries and commissions	\$7.1	\$7.3	\$(0.2)	(2.2)%
Other operating expenses	6.0	6.3	(0.3)	(5.3)%
Depreciation and amortization	0.7	0.7	—	(0.7)%
Total operating expenses	\$13.8	\$14.3	\$(0.5)	(3.5)%
Operating expenses as a percent of sales	21.2%	18.3%	2.9	%

Note: Due to rounding, numbers may not add up to total operating expenses.

Salaries and commissions decreased \$0.2 million between the periods primarily due to a headcount reduction.

Other operating expenses decreased \$0.3 million as facility costs decreased due to rationalization and lower employee related expenses including healthcare, offset by increased professional fees, due to the Vertex acquisition and other administrative expenses.

Depreciation and amortization remained consistent between the periods.

Operating expenses as a percentage of sales increased to 21.2% in 2016 from 18.3% in 2015, as sales levels fell at a greater rate than the reduction in operating expenses.

Interest Expense

Interest expense decreased 45.6% from \$0.2 million in 2015 to \$0.1 million in 2016 due to lower average debt levels and lower interest rates. Average debt was \$28.5 million in 2016 compared to \$41.5 million in 2015. The average effective interest rate was 1.7% in 2016 compared to 2.2% in 2015.

Income Taxes

We recorded an income tax benefit of \$0.5 million in 2016, due to the pre-tax loss, compared to the \$0.9 million income tax expense in the prior year period. The effective income tax rate decreased to 25.6% in 2016 from 56.3% in 2015. The 2016 income tax benefit was net of a \$0.2 million charge resulting from the write-off of deferred tax assets related to share-based awards that vested or were forfeited during the quarter. In 2015, the effective tax rate for the third quarter was impacted by the non-deductible goodwill impairment. If the Company's stock price remains below the grant-date values of share-based compensation, future forfeitures, vesting and exercises will result in charges to income tax expense, which will negatively impact the effective tax rate.

Net Income (Loss)

We incurred a net loss of \$1.4 million in 2016 compared to net income of \$0.7 million in 2015, primarily due to the decline in sales and the resulting decrease in gross profit.

Comparison of the Nine Months Ended September 30, 2016 and 2015**Sales**

	Nine Months Ended September 30,		
(Dollars in millions)	2016	2015	Change
Sales	\$192.4	\$237.8	\$(45.4) (19.1)%

Our sales for the nine month period decreased 19.1% to \$192.4 million in 2016 from \$237.8 million in 2015. We estimate that, when adjusted for the fluctuation in metal prices, sales for 2016 were down approximately 11% compared to the first nine months of 2015. Our project business, which targets end markets encompassing Environmental Compliance, Engineering & Construction, Industrials, Utility Power Generation, and Mechanical Wire Rope, is estimated to have decreased 38%, or approximately 30% on a metals adjusted basis, from 2015. MRO sales fell 10%, or approximately 2% when adjusted for metals, from 2015.

Gross Profit

	Nine Months Ended September 30,		
(Dollars in millions)	2016	2015	Change
Gross profit	\$37.9	\$50.8	\$(12.9) (25.4)%
Gross margin	19.7%	21.4%	(1.7)%

Gross profit decreased 25.4% to \$37.9 million in 2016 from \$50.8 million in 2015. The decrease in gross profit was primarily attributable to the lower sales in 2016. Gross margin decreased to 19.7% in 2016 from 21.4% in 2015, primarily due to competitive market conditions.

Operating Expenses

	Nine Months Ended September 30,		
(Dollars in millions)	2016	2015	Change

Edgar Filing: Houston Wire & Cable CO - Form 10-Q

Operating expenses:

Salaries and commissions	\$20.9	\$21.7	\$(0.8)	(3.8)%
Other operating expenses	17.3	18.6	(1.3)	(7.1)%
Depreciation and amortization	2.2	2.2	—	1.1 %
Impairment charge	2.4	3.0	(0.6)	(20.4)%
Total operating expenses	\$42.8	\$45.5	\$(2.7)	(6.0)%

Operating expenses as a percent of sales 22.2% 19.1% 3.1 %

Note: Due to rounding, numbers may not add up to total operating expenses.

Salaries and commissions decreased \$0.8 million between the periods as sales and gross margin levels declined reducing commissions and due to a lower headcount.

Other operating expenses decreased \$1.3 million due to a decrease in facility occupancy costs, lower employee related expenses including healthcare due to a lower headcount and the absence of moving costs incurred with the 2015 consolidation of the Southwest Houston facilities, offset by increased professional fees due to the Vertex acquisition.

Depreciation and amortization remained consistent between the periods.

The impairment charge in 2016 relates to the write-off of goodwill on the HWC reporting unit and the write-down of tradenames at the Southern Wire reporting unit. In 2015 the impairment consisted of the write-off of goodwill at the Southwest reporting unit and the write-down of tradenames at the Southwest and Southern Wire reporting units. (See Note 3)

Operating expenses as a percentage of sales increased to 22.2% in 2016 from 19.1% in 2015, as sales levels fell at a greater rate than the reduction in operating expenses.

Interest Expense

Interest expense decreased 37.0% to \$0.5 million in 2016 from \$0.7 million in 2015 due to lower average debt levels and lower interest rates. Average debt was \$32.4 million in 2016 compared to \$45.2 million in 2015. The average effective interest rate fell to 1.7% in 2016 from 2.1% in the prior year period.

Income Taxes

The income tax benefit of \$1.2 million changed from the \$2.3 million expense in 2015, primarily due to the pre-tax loss incurred in the 2016 period. The effective income tax rate decreased to 22.0% in 2016 from 50.8% in 2015. The 2016 rate was impacted by the \$0.3 million charge resulting from the write-off of deferred tax assets related to share-based awards that vested or were forfeited in 2016 and the non-deductible portion of the goodwill impairment of \$0.5 million. The 2015 rate of 50.8% was due to the non-deductible portion of the impairment charge.

Net Income (Loss)

We incurred a net loss of \$4.2 million in 2016 compared to net income of \$2.2 million in 2015, which was due to the sales shortfall and the resulting decrease in gross profit.

Impact of Inflation and Commodity Prices

Our results of operations are affected by changes in the inflation rate and commodity prices. Moreover, because copper, steel, aluminum and petrochemical products are components of the wire and cable and related hardware we sell, fluctuations in the costs of these and other commodities have historically affected our operating results. To the extent commodity prices decline, the net realizable value of our existing inventory could also decline, and our gross profit could be adversely affected because of either reduced selling prices or lower of cost or market adjustments in the carrying value of our inventory. If we turn our inventory approximately three times a year, the impact of changes in commodity prices in any particular quarter would primarily affect the results of the succeeding two calendar quarters. If we are unable to pass on to our customers future cost increases due to inflation or rising commodity prices, our operating results could be adversely affected.

Liquidity and Capital Resources

Our primary capital needs are for working capital obligations, capital expenditures, dividend payments, our stock repurchase program and other general corporate purposes, including acquisitions. Our primary sources of working capital are cash from operations supplemented by bank borrowings.

Liquidity is defined as the ability to generate adequate amounts of cash to meet the current need for cash. We assess our liquidity in terms of our ability to generate cash to fund our operating activities. Significant factors which could affect liquidity include the following:

- the adequacy of available bank lines of credit;
- cash flows generated from operating activities;
- capital expenditures;
- additional stock repurchases;
- payment of dividends;
- acquisitions; and
- the ability to attract long-term capital with satisfactory terms

Comparison of the Nine Months Ended September 30, 2016 and 2015

Our net cash provided by operating activities was \$16.0 million for the nine months ended September 30, 2016 compared to \$28.8 million in 2015. We had a net loss of \$4.2 million in 2016 compared to net income of \$2.2 million in 2015.

Changes in our operating assets and liabilities provided cash from operating activities of \$15.3 million in 2016. A reduction in our inventory investment of \$11.9 million as inventory profiles were reduced to align with current activity levels, a decrease in accounts receivables of \$3.4 million due to the decrease in sales and an increase in accounts payable of \$2.1 million were the main sources of cash. Partially offsetting these sources of cash was the reduction of the book overdraft of \$2.6 million.

Net cash used in investing activities was \$1.0 million in 2016 compared to \$2.9 million in 2015. The decrease was primarily attributable to the renovation costs of the Southwest Wire Rope facility consolidation in 2015 and miscellaneous equipment purchases.

Net cash used in financing activities was \$15.0 million in 2016 compared to \$25.8 million in 2015. Net payments on the revolver of \$10.6 million, the payment of dividends of \$2.5 million and the purchase of treasury stock of \$2.0 million were the components of financing activities in 2016.

Indebtedness

Our principal source of liquidity at September 30, 2016 was working capital of \$88.5 million compared to \$104.0 million at December 31, 2015. We also had additional available borrowing capacity of approximately \$44.8 million at September 30, 2016 and \$41.5 million at December 31, 2015 under our loan agreement. The availability at September 30, 2016 is net of outstanding letters of credit of less than \$0.1 million.

On October 3, 2016, we purchased Vertex, which was funded under the amended 2015 Loan Agreement. See Note 8.

We believe that we will have adequate availability of capital to fund our present operations, meet our commitments on our existing debt, fund our dividend payments and stock repurchase program, and fund anticipated growth over the next twelve months, including expansion in existing and targeted market areas. We continually seek potential acquisitions and from time to time hold discussions with acquisition candidates. If suitable acquisition opportunities or working capital needs arise that would require additional financing, we believe that our financial position and earnings history provide a solid base for obtaining additional financing resources at competitive rates and terms. Additionally, based on market conditions, we may decide to issue additional shares of common or preferred stock to raise funds.

Contractual Obligations

The following table summarizes our loan commitment at September 30, 2016:

In millions	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Total debt	\$28.6	\$ —	\$ —	\$ 28.6	\$ —

There were no material changes in operating lease obligations or non-cancellable purchase obligations since December 31, 2015.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

There were no material changes to our market risk as set forth in Items 7A and 7 of our Annual Report on Form 10-K for the year ended December 31, 2015.

Item 4. Controls and Procedures

As of September 30, 2016, an evaluation was performed by the Company's management, under the supervision and with the participation of the Company's chief executive officer and chief financial officer, of the effectiveness of the Company's disclosure controls and procedures. Based on that evaluation, the chief executive officer and the chief financial officer concluded that the Company's disclosure controls and procedures were effective. There were no changes in the Company's internal control over financial reporting that occurred during the quarter ended September 30, 2016 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Part II. Other Information

Item 1 – Not applicable and has been omitted.

Item 1A. Risk Factors

There were no material changes in the risk factors disclosed in our Annual Report on Form 10-K for the year ended December 31, 2015.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The following table provides information about our purchases of common stock for the three months ended September 30, 2016.

Period	Total number of shares purchased	Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs ⁽¹⁾	Maximum dollar value that may yet be used for purchases under the plan ⁽¹⁾
July 1 – 31, 2016	19,310	\$ 5.77	19,310	\$9,861,434
August 1 – 31, 2016	36,622	5.75	36,622	9,650,988
September 1 – 30, 2016	35,590	5.91	35,590	9,440,793
Total	91,522	\$ 5.81	91,522	

⁽¹⁾ The board authorized a stock repurchase program of \$25 million in March 2014. The program has no expiration date.

Item 3 – Not applicable and has been omitted.

Item 4 – Not applicable and has been omitted.

Item 5 – Not applicable and has been omitted.

Item 6. Exhibits

(a) Exhibits required by Item 601 of Regulation S-K.

Exhibit Number	Document Description
31.1	Certification by James L. Pokluda III pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification by Nicol G. Graham pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification by James L. Pokluda III and Nicol G. Graham pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document ⁽¹⁾
101.SCH	XBRL Taxonomy Extension Schema
101.CAL	XBRL Taxonomy Extension Calculation Linkbase
101.DEF	XBRL Taxonomy Extension Definition Linkbase
101.LAB	XBRL Taxonomy Extension Label Linkbase
101.PRE	XBRL Taxonomy Extension Presentation Linkbase

Attached as exhibit 101 to this report are the following documents formatted in XBRL (Extensible Business Reporting Language): (i) the Consolidated Balance Sheets at September 30, 2016 and December 31, 2015; (ii) the (1) Consolidated Statements of Operations for the three month and nine month periods ended September 30, 2016 and 2015; (iii) the Consolidated Statements of Cash Flows for the nine month periods ended September 30, 2016 and 2015; and (vi) Notes to the Consolidated Financial Statements.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: November 8, 2016 **HOUSTON WIRE & CABLE COMPANY**

BY: /s/ Nicol G. Graham

Nicol G. Graham, Chief Financial Officer

EXHIBIT INDEX

Exhibit Number	Document Description
31.1	Certification by James L. Pokluda III pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification by Nicol G. Graham pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification by James L. Pokluda III and Nicol G. Graham pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document ⁽¹⁾
101.SCH	XBRL Taxonomy Extension Schema
101.CAL	XBRL Taxonomy Extension Calculation Linkbase
101.DEF	XBRL Taxonomy Extension Definition Linkbase
101.LAB	XBRL Taxonomy Extension Label Linkbase
101.PRE	XBRL Taxonomy Extension Presentation Linkbase

Attached as exhibit 101 to this report are the following documents formatted in XBRL (Extensible Business Reporting Language): (i) the Consolidated Balance Sheets at September 30, 2016 and December 31, 2015; (ii) the Consolidated Statements of Operations for the three month and nine month periods ended September 30, 2016 and 2015; (iii) the Consolidated Statements of Cash Flows for the nine month periods ended September 30, 2016 and 2015; and (vi) Notes to the Consolidated Financial Statements.