SKECHERS USA INC
Form 10-Q
August 07, 2009

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2009

OR

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES AND EXCHANGE ACT OF 1934**

For the transition period from __________ to __________

Commission File Number 001-14429
SKECHERS U.S.A., INC.
(Exact name of registrant as specified in its charter)

Delaware **(State or Other Jurisdiction of Incorporation or Organization)**	**95-4376145** **(I.R.S. Employer Identification No.)**
228 Manhattan Beach Blvd. **Manhattan Beach, California** **(Address of Principal Executive Office)**	**90266** **(Zip Code)**

(310) 318-3100
(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 þ Noo

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 o Noo

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 definitions of large accelerated filer , accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer þ	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

THE NUMBER OF SHARES OF CLASS A COMMON STOCK OUTSTANDING AS OF AUGUST 1, 2009: 33,649,737.

THE NUMBER OF SHARES OF CLASS B COMMON STOCK OUTSTANDING AS OF AUGUST 1, 2009: 12,738,483.

SKECHERS U.S.A., INC. AND SUBSIDIARIES
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PART I FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

SKECHERS U.S.A., INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

(In thousands)

	June 30, 2009	December 31, 2008
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 257,024	$ 114,941
Trade accounts receivable, less allowances of $11,848 in 2009 and $14,880 in 2008	193,729	175,064
Other receivables	10,713	7,816
Total receivables	204,442	182,880
Inventories	191,283	261,209
Prepaid expenses and other current assets	31,991	31,022
Deferred tax assets	11,955	11,955
Total current assets	696,695	602,007
Property and equipment, at cost, less accumulated depreciation and amortization	174,411	157,757
Intangible assets, less accumulated amortization	5,036	5,407
Deferred tax assets	12,609	18,158
Long-term marketable securities		81,925
Other assets, at cost	12,450	11,062
TOTAL ASSETS	$ 901,201	$ 876,316
LIABILITIES AND EQUITY		
Current Liabilities:		
Current installments of long-term borrowings	642	572
Short-term borrowings	639	
Accounts payable	178,066	164,643
Accrued expenses	16,764	23,021
Total current liabilities	196,111	188,236
Long-term borrowings, excluding current installments	15,858	16,188
Total liabilities	211,969	204,424
Commitments and contingencies		
Equity:		
Preferred Stock, $.001 par value; 10,000 authorized; none issued and outstanding		
Class A Common Stock, $.001 par value; 100,000 shares authorized; 33,647 and 33,410 shares issued and outstanding at June 30, 2009 and December 31, 2008,	33	33

respectively		
Class B Common Stock, $.001 par value; 100,000 shares authorized; 12,738 and 12,782 shares issued and outstanding at June 30, 2009 and December 31, 2008, respectively	13	13
Additional paid-in capital	265,763	264,200
Accumulated other comprehensive income (loss)	7,306	(4,719)
Retained earnings	411,460	409,166
Skechers U.S.A., Inc. equity	684,575	668,693
Noncontrolling interest	4,657	3,199
Total equity	689,232	671,892
TOTAL LIABILITIES AND EQUITY	$ 901,201	$ 876,316

See accompanying notes to unaudited condensed consolidated financial statements.

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SKECHERS U.S.A., INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
(Unaudited)
(In thousands, except per share data)

	Three-Months Ended June 30,		Six-Months Ended June 30,	
	2009	2008	2009	2008
Net sales	$ 298,976	$ 354,574	$ 642,446	$ 739,496
Cost of sales	176,373	197,381	394,414	410,131
Gross profit	122,603	157,193	248,032	329,365
Royalty income	332	230	604	1,070
	122,935	157,423	248,636	330,435
Operating expenses:				
Selling	34,813	38,592	56,323	64,126
General and administrative	95,848	98,857	193,886	198,079
	130,661	137,449	250,209	262,205
Earnings (loss) from operations	(7,726)	19,974	(1,573)	68,230
Other income (expense):				
Interest income	581	1,835	1,290	4,294
Interest expense	(912)	(1,347)	(957)	(2,353)
Other, net	245	844	27	748
	(86)	1,332	360	2,689
Earnings (loss) before income taxes (benefit)	(7,812)	21,306	(1,213)	70,919
Income tax (benefit) expense	(1,186)	7,045	(1,939)	23,814
Net earnings (loss)	(6,626)	14,261	726	47,105
Less: Net loss attributable to noncontrolling interest	(699)	(380)	(1,567)	(380)
Net earnings (loss) attributable to Skechers U.S.A., Inc.	$ (5,927)	$ 14,641	$ 2,293	$ 47,485
Net earnings (loss) per share attributable to Skechers U.S.A., Inc.:				
Basic	$ (0.13)	$ 0.32	$ 0.05	$ 1.03

Diluted	$ (0.13)	$ 0.31	$ 0.05	$ 1.02
Weighted average shares used in calculating earnings per share attributable to Skechers U.S.A., Inc.:				
Basic	46,282	46,000	46,252	45,941
Diluted	46,282	46,810	46,424	46,737
Comprehensive income:				
Net earnings (loss)	$ (5,927)	$ 14,641	$ 2,293	$ 47,485
Unrealized gain (loss) on marketable securities, net of tax	10,234	(2,559)	8,151	(3,906)
Gain (loss) on foreign currency translation adjustment, net of tax	6,836	(159)	3,874	890
Total comprehensive income	$ 11,143	$ 11,923	$ 14,318	$ 44,469

See accompanying notes to unaudited condensed consolidated financial statements.

SKECHERS U.S.A., INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In thousands)

	Six-Months Ended June 30, 2009	Six-Months Ended June 30, 2008
Cash flows from operating activities:		
Net earnings	$ 2,293	$ 47,485
Adjustments to reconcile net earnings to net cash provided by (used in) operating activities:		
Noncontrolling interest in subsidiaries	(1,567)	(380)
Depreciation of property and equipment	9,337	8,715
Amortization of intangible assets	410	119
Provision (recoveries) for bad debts and returns	(352)	4,954
Tax benefits from stock-based compensation		533
Non-cash stock compensation	1,210	1,127
Loss on disposal of property and equipment	2	1,538
Provision for deferred income taxes	(605)	
Impairment of property and equipment	761	
(Increase) decrease in assets:		
Receivables	(17,288)	(68,316)
Inventories	71,199	(29,841)
Prepaid expenses and other current assets	(548)	(6,819)
Other assets	(1,357)	(16,231)
Increase (decrease) in liabilities:		
Accounts payable	11,012	19,655
Accrued expenses	(6,173)	10,929
Net cash provided by (used in) operating activities	68,334	(26,532)
Cash flows from investing activities:		
Capital expenditures	(26,860)	(37,838)
Purchases of investments		(11,725)
Maturities of investments	375	16,250
Redemption of auction rate securities	95,250	
Net cash provided by (used in) investing activities	68,765	(33,313)
Cash flows from financing activities:		
Net proceeds from the issuances of stock through employee stock purchase plan and the exercise of stock options	958	2,812
Payments on long-term debt	(166)	(407)
Increase in short-term borrowings	639	
Contribution from noncontrolling interest of consolidated entity	3,000	3,000
Excess tax benefits from stock-based compensation		528
Net cash provided by financing activities	4,431	5,933

Net increase (decrease) in cash and cash equivalents	141,530	(53,912)
Effect of exchange rates on cash and cash equivalents	553	18
Cash and cash equivalents at beginning of the period	114,941	199,516
Cash and cash equivalents at end of the period	$ 257,024	$ 145,622
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest, net of amounts capitalized	$ 1,978	$ 2,527
Income taxes	1,030	13,875

See accompanying notes to unaudited condensed consolidated financial statements.

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SKECHERS U.S.A., INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2009 and 2008
(Unaudited)

(1) GENERAL

Basis of Presentation

The accompanying condensed consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include certain footnotes and financial presentations normally required under accounting principles generally accepted in the United States of America for complete financial reporting. The interim financial information is unaudited, but reflects all normal adjustments and accruals which are, in the opinion of management, considered necessary to provide a fair presentation for the interim periods presented. The accompanying condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements included in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2008.

The results of operations for the six months ended June 30, 2009 are not necessarily indicative of the results to be expected for the entire fiscal year ending December 31, 2009.

Use of Estimates

The preparation of the condensed consolidated financial statements, in conformity with accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

Noncontrolling interests

On January 1, 2009, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 160, *Noncontrolling Interests in Consolidated Financial Statements, and amendment of ARB no. 51* (SFAS 160). The objective of SFAS 160 is to improve the relevance, comparability, and transparency of the financial information that a reporting entity provides in its consolidated financial statements by establishing accounting and reporting standards for noncontrolling interests in a subsidiary and for the deconsolidation of a subsidiary. Under the provisions of this statement, the income statement presentation has been revised to separately present consolidated net income, which now includes the amounts attributable to the Company, plus noncontrolling interests and net income attributable solely to the Company. Noncontrolling interest, previously referred to as minority interest, in the Company s consolidated financial statements results from the accounting for a noncontrolling interest in a consolidated subsidiary or affiliate. Noncontrolling interest represents partially-owned subsidiaries or consolidated affiliate s income, losses, and components of other comprehensive income (loss) which is attributable to the noncontrolling parties interests. In addition, noncontrolling interests are considered a component of equity for all periods presented. Noncontrolling interests were previously classified within other long-term liabilities. Prior year presentations have been reclassified to conform with these requirements.

The Company has a 50 percent interest in Skechers China Limited (Skechers China), a joint venture which was formed in October 2007, and made a capital contribution of cash and inventory of $3.0 million during the six months ended June 30, 2009. Our joint venture partner also made a corresponding cash capital contribution during the six months ended June 30, 2009. The Company also has a 50 percent interest in Skechers Southeast Asia Limited (Skechers Southeast Asia) and Skechers (Thailand) Ltd. (Skechers Thailand). The Company consolidates these joint ventures into its financial statements because it holds a majority of seats on the board of directors and, thus, controls the joint ventures. Net loss attributable to noncontrolling interest of $0.7 million for the three months ended June 30, 2009 and $1.6 million for the six months ended June 30, 2009 represents the share of net loss that is attributable to the equity of these joint ventures that is owned by our joint venture partners. Transactions between these joint ventures and Skechers have been eliminated in the consolidated financial statements.

Recent accounting pronouncements

In June 2009, the FASB approved the FASB Accounting Standards Codification, or the Codification, as the single source of authoritative nongovernmental Generally Accepted Accounting Principles, or GAAP, in the United States. The Codification will be effective for interim and annual periods ending after September 15, 2009. Upon the effective date, the Codification will be the single source of authoritative accounting principles to be applied by all nongovernmental United States entities. All other accounting literature not included in the Codification will be nonauthoritative. Adoption of this standard will change future authoritative accounting literature references included in our financial statements to be in accordance with the Codification.

(2) INVESTMENTS

During the second quarter of 2009, Wachovia Securities purchased $95.3 million of the Company s investments in auction rate preferred stocks and auction rate Dividend Received Deduction (DRD) preferred securities at par for cash. At December 31, 2008, long-term investments were $81.9 million net of unrealized losses of $13.7 million.

(3) REVENUE RECOGNITION

The Company recognizes revenue on wholesale sales when products are shipped and the customer takes title and assumes risk of loss, collection of relevant receivable is reasonably assured, persuasive evidence of an arrangement exists and the sales price is fixed or determinable. This generally occurs at time of shipment. The Company recognizes revenue from retail sales at the point of sale. Allowances for estimated returns, discounts, doubtful accounts and chargebacks are provided for when related revenue is recorded. Related costs paid to third-party shipping companies are recorded as a cost of sales.

Royalty income is earned from licensing arrangements. Upon signing a new licensing agreement, we receive up-front fees, which are generally characterized as prepaid royalties. These fees are initially deferred and recognized as revenue as earned (i.e., as licensed sales are reported to the company or on a straight-line basis over the term of the agreement). The first calculated royalty payment is based on actual sales of the licensed product. Typically, at each quarter-end we receive correspondence from our licensees indicating the actual sales for the period. This information is used to calculate and accrue the related royalties based on the terms of the agreement.

(4) OTHER COMPREHENSIVE INCOME

In addition to net earnings (loss), other comprehensive income includes changes in foreign currency translation adjustments and unrealized gains and losses on marketable securities. The Company operates internationally through several foreign subsidiaries. Assets and liabilities of the foreign operations denominated in local currencies are translated at the rate of exchange at the balance sheet date. Revenues and expenses are translated at the weighted average rate of exchange during the period of translation. The resulting translation adjustments along with the translation adjustments related to intercompany loans of a long-term investment nature are included in the translation adjustment in other comprehensive income.

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The activity in other comprehensive income, net of income taxes, was as follows (in thousands):

	Three-Months Ended June 30, 2009	Six-Months Ended June 30, 2009
Net earnings (loss)	$ (6,626)	$ 726
Unrealized gain on marketable securities, net of tax	10,234	8,151
Gain on foreign currency translation adjustment, net of tax	6,881	3,899
Comprehensive income	10,489	12,776
Comprehensive loss attributable to noncontrolling interest	(654)	(1,542)
Comprehensive income attributable to parent	$ 11,143	$ 14,318

(5) STOCK COMPENSATION

For stock-based awards we have recognized compensation expense based on the estimated grant date fair value using the Black-Scholes valuation model, which requires the input of highly subjective assumptions including the expected stock price volatility, expected term and forfeiture rate. Stock compensation expense was $0.6 million and $0.6 million for the three months ended June 30, 2009 and 2008, respectively. Stock compensation expense was $1.2 million and $1.1 million for the six months ended June 30, 2009 and 2008, respectively.

Stock options granted pursuant to the 1998 Stock Option, Deferred Stock and Restricted Stock Plan and the 2007 Incentive Award Plan (the Equity Incentive Plan) were as follows:

	SHARES	WEIGHTED AVERAGE EXERCISE PRICE	WEIGHTED AVERAGE REMAINING CONTRACTUAL TERM	AGGREGATE INTRINSIC VALUE
Outstanding at December 31, 2008	1,739,721	$ 11.79		
Granted				
Exercised	(23,618)	7.64		
Cancelled	(107,817)	11.21		
Outstanding at June 30, 2009	1,608,286	11.89	2.4 years	$1,504,895
Exercisable at June 30, 2009	1,608,286	11.89	2.4 years	$1,504,895

A summary of the status and changes of our nonvested shares related to the Equity Incentive Plan as of and during the six months ended June 30, 2009 is presented below:

	SHARES	WEIGHTED AVERAGE GRANT-DATE FAIR VALUE
Nonvested at December 31, 2008	217,284	$ 16.97
Granted	2,500	12.22

Vested	(101,807)	17.10
Cancelled		
Nonvested at June 30, 2009	117,977	16.76

(6) EARNINGS (LOSS) PER SHARE

Basic earnings (loss) per share represents net earnings divided by the weighted average number of common shares outstanding for the period. Diluted earnings per share, in addition to the weighted average determined for basic earnings (loss) per share, includes potential common shares, if dilutive, which would arise from the exercise of stock options and nonvested shares using the treasury stock method.

Net earnings for the six months ended June 30, 2009 were positively impacted by a $1.9 million adjustment for a discrete tax item as discussed in Note 7, Income Taxes.

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The following is a reconciliation of net earnings (loss) and weighted average common shares outstanding for purposes of calculating basic earnings per share (in thousands, except per share amounts):

	Three-Months Ended June 30,		Six-Months Ended June 30,	
Basic earnings (loss) per share	**2009**	**2008**	**2009**	**2008**
Net earnings (loss) attributable to Skechers U.S.A., Inc.	$ (5,927)	$14,641	$ 2,293	$47,485
Weighted average common shares outstanding	46,282	46,000	46,252	45,941
Basic earnings (loss) per share attributable to Skechers U.S.A., Inc.	$ (0.13)	$ 0.32	$ 0.05	$ 1.03

The following is a reconciliation of net earnings (loss) and weighted average common shares outstanding for purposes of calculating diluted earnings per share (in thousands, except per share amounts):

	Three-Months Ended June 30,		Six-Months Ended June 30,	
Diluted earnings (loss) per share	**2009**	**2008**	**2009**	**2008**
Net earnings (loss) attributable to Skechers U.S.A., Inc.	$ (5,927)	$ 14,641	$ 2,293	$ 47,485
Weighted average common shares outstanding	46,282	46,000	46,252	45,941
Dilutive effect of stock options		810	172	796
Weighted average common shares outstanding	46,282	46,810	46,424	46,737
Diluted earnings (loss) per share attributable to Skechers U.S.A., Inc.	$ (0.13)	$ 0.31	$ 0.05	$ 1.02

Options to purchase 993,742 and 156,016 shares of Class A common stock were not included in the computation of diluted earnings (loss) per share for the three months ended June 30, 2009 and 2008, respectively, because their effect would have been anti-dilutive. Options to purchase 995,742 and 156,016 shares of Class A common stock were not included in the computation of diluted earnings per share for the six months ended June 30, 2009 and 2008, respectively, because their effect would have been anti-dilutive.

(7) INCOME TAXES

The Company s effective tax rate was 15.2% and 33.1% for the three months ended June 30, 2009 and 2008, respectively. The Company s effective tax rate was 159.9% and 33.6% for the six months ended June 30, 2009 and 2008, respectively. The rate for the six months ended June 30, 2009 is greater than the expected domestic rate of approximately 40% due to the inclusion of the $1.9 million discrete tax benefit adjusting the amount of tax benefit recognized in 2008 relating to the Company entering into an advanced pricing agreement (APA) with the U.S. Internal Revenue Service (IRS). Excluding this discrete item, the Company s effective tax rate for the six months ended June 30, 2009 would have been (0.7%), which is lower than the expected domestic rate of approximately 40% due to our non-U.S. subsidiary earnings in lower tax rate jurisdictions and our planned permanent reinvestment of undistributed earnings from our non-U.S. subsidiaries, thereby indefinitely postponing their repatriation to the United States. As such, the Company did not provide for deferred income taxes on accumulated undistributed earnings of our non-U.S. subsidiaries.

Accounting Principles Board Opinion No. 28, *Interim F*