SKECHERS USA INC
Form 10-Q
August 06, 2010

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, 2010

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

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 No o

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 o	Accelerated filer þ	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 2, 2010: 36,166,847.

THE NUMBER OF SHARES OF CLASS B COMMON STOCK OUTSTANDING AS OF AUGUST 2, 2010: 11,390,610.

SKECHERS U.S.A., INC. AND SUBSIDIARIES
FORM 10-Q
TABLE OF CONTENTS

PART I FINANCIAL INFORMATION

PART II OTHER INFORMATION

Table of Contents

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, 2010	December 31, 2009
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 273,266	$ 265,675
Short-term investments	0	30,000
Trade accounts receivable, net	304,992	219,924
Other receivables	7,526	12,177
Total receivables	312,518	232,101
Inventories	219,360	224,050
Prepaid expenses and other current assets	30,012	28,233
Deferred tax assets	8,950	8,950
Total current assets	844,106	789,009
Property and equipment, at cost, less accumulated depreciation and amortization	236,709	171,667
Intangible assets, less accumulated amortization	8,147	9,011
Deferred tax assets	13,667	13,660
Other assets, at cost	33,213	12,205
TOTAL ASSETS	$ 1,135,842	$ 995,552
LIABILITIES AND EQUITY		
Current Liabilities:		
Short-term borrowings	$ 1,956	$ 2,006
Current installments of long-term borrowings	15,899	529
Accounts payable	191,653	196,163
Accrued expenses	22,142	31,843
Total current liabilities	231,650	230,541
Long-term borrowings, excluding current installments	14,532	15,641
Total liabilities	246,182	246,182
Commitments and contingencies		
Equity:		
Preferred Stock, $.001 par value; 10,000 authorized; none issued and outstanding	0	0
	36	34

Class A Common Stock, $.001 par value; 100,000 shares authorized; 36,204 and 34,229 shares issued and outstanding at June 30, 2010 and December 31, 2009, respectively respectively		
Class B Common Stock, $.001 par value; 100,000 shares authorized; 11,346 and 12,360 shares issued and outstanding at June 30, 2010 and December 31, 2009, respectively respectively	11	13
Additional paid-in capital	295,857	272,662
Accumulated other comprehensive income (loss)	(1,067)	9,348
Retained earnings	560,398	463,865
Skechers U.S.A., Inc. equity	855,235	745,922
Noncontrolling interests	34,425	3,448
Total equity	889,660	749,370
TOTAL LIABILITIES AND EQUITY	$ 1,135,842	$ 995,552

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents

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,	
	2010	**2009**	**2010**	**2009**
Net sales	$ 504,859	$ 298,976	$ 997,623	$ 642,446
Cost of sales	267,214	176,373	522,560	394,414
Gross profit	237,645	122,603	475,063	248,032
Royalty income	875	332	1,260	604
	238,520	122,935	476,323	248,636
Operating expenses:				
Selling	52,437	34,813	86,746	56,323
General and administrative	127,299	95,848	249,786	193,886
	179,736	130,661	336,532	250,209
Earnings (loss) from operations	58,784	(7,726)	139,791	(1,573)
Other income (expense):				
Interest income	436	581	1,864	1,290
Interest expense	(118)	(912)	(833)	(957)
Other, net	1,611	245	1,820	27
	1,929	(86)	2,851	360
Earnings (loss) before income taxes (benefit)	60,713	(7,812)	142,642	(1,213)
Income tax expense (benefit)	20,396	(1,186)	46,202	(1,939)
Net earnings (loss)	40,317	(6,626)	96,440	726
Less: Net earnings (loss) attributable to noncontrolling interests	80	(699)	(93)	(1,567)
Net earnings (loss) attributable to Skechers U.S.A., Inc.	$ 40,237	$ (5,927)	$ 96,533	$ 2,293
Net earnings (loss) per share attributable to Skechers U.S.A., Inc.:				
Basic	$ 0.85	$ (0.13)	$ 2.05	$ 0.05
Diluted	$ 0.82	$ (0.13)	$ 1.97	$ 0.05

Weighted average shares used in calculating earnings (loss) per share attributable to Skechers U.S.A., Inc.:				
Basic	47,422	46,282	47,107	46,252
Diluted	49,130	46,282	48,955	46,424
Comprehensive income:				
Net earnings (loss)	$ 40,237	$ (5,927)	$ 96,533	$ 2,293
Unrealized gain on marketable securities, net of tax	0	10,234	0	8,151
Gain (loss) on foreign currency translation adjustment, net of tax	(6,147)	6,836	(10,415)	3,874
Total comprehensive income	$ 34,090	$ 11,143	$ 86,118	$ 14,318

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents

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

	Six-Months Ended June 30, 2010	2009
Cash flows from operating activities:		
Net earnings	$ 96,533	$ 2,293
Adjustments to reconcile net earnings to net cash provided by (used in) operating activities:		
Noncontrolling interest in subsidiaries	(93)	(1,567)
Depreciation of property and equipment	10,870	9,337
Amortization of deferred financing costs	741	0
Amortization of intangible assets	892	410
Provision (recoveries) for bad debts and returns	3,135	(352)
Tax benefits from stock-based compensation	0	0
Non-cash stock compensation	6,665	1,210
Loss on disposal of property and equipment	50	2
Deferred taxes	(12)	(605)
Impairment of property and equipment	0	761
(Increase) decrease in assets:		
Receivables	(91,260)	(17,288)
Inventories	3,718	71,199
Prepaid expenses and other current assets	(2,215)	(548)
Other assets	(22,555)	(1,357)
Increase (decrease) in liabilities:		
Accounts payable	(5,058)	11,012
Accrued expenses	(9,381)	(6,173)
Net cash provided by (used in) operating activities	(7,970)	68,334
Cash flows from investing activities:		
Capital expenditures	(29,721)	(26,860)
Maturities of investments	30,000	375
Redemption of auction rate securities	0	95,250
Intangible additions	(31)	0
Net cash provided by investing activities	248	68,765
Cash flows from financing activities:		
Net proceeds from the issuances of stock through employee stock purchase plan and the exercise of stock options	10,772	958
Payments on long-term debt	(281)	(166)
Increase (decrease) in short-term borrowings	(61)	639
Capital contribution from noncontrolling interest of consolidated entity	1,000	3,000
Excess tax benefits from stock-based compensation	5,758	
Net cash provided by financing activities	17,188	4,431

Net increase in cash and cash equivalents	9,466	141,530
Effect of exchange rates on cash and cash equivalents	(1,875)	553
Cash and cash equivalents at beginning of the period	265,675	114,941
Cash and cash equivalents at end of the period	$ 273,266	$ 257,024
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest	$ 1,512	$ 1,978
Income taxes	53,343	1,030
Non-cash transactions:		
Land contribution from noncontrolling interest of consolidated entity	30,000	0
Note payable contribution from noncontrolling interest of consolidated entity	14,567	0

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents

SKECHERS U.S.A., INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2010 and 2009
(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 material normal recurring 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, 2009.

The results of operations for the six months ended June 30, 2010 are not necessarily indicative of the results to be expected for the entire fiscal year ending December 31, 2010.

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

The Company has interests in certain joint ventures which are consolidated into its financial statements. Noncontrolling interest was income of $0.1 million and loss of $0.7 million for the three months ended June 30, 2010 and 2009, respectively, which represents the share of net earnings or loss that is attributable to our joint venture partners. Noncontrolling interest was loss of $0.1 million and a loss of $1.6 million for the six months ended June 30, 2010 and 2009, respectively. Our joint venture partners made a $30.0 million capital contribution in land and a cash capital contribution of $1.0 million during the six months ended June 30, 2010.

For the period ended June 30, 2010, the Company has determined that its joint venture with HF Logistics I, LLC (HF) is a variable interest entity (VIE) and that the Company is the primary beneficiary. The VIE is consolidated into the condensed consolidated financial statements and the carrying amounts and classification of assets and liabilities was as follows (in millions):

	June 30, 2010	December 31, 2009
Current assets	$ 4,178	$ 0
Noncurrent assets	75,990	0
Total assets	$ 80,168	$ 0
Current liabilities	$ 5,584	$ 0
Noncurrent liabilities	14,567	0
Total liabilities	$ 20,151	$ 0

6

Table of Contents

The Company did not have a significant variable interest in any unconsolidated VIE s.

Recent accounting pronouncements

In June 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2009-17, *Amendments to FASB Interpretation No. 46(R)*. ASU 2009-17 requires a qualitative approach to identifying a controlling financial interest in a VIE, and requires ongoing assessment of whether an entity is a VIE and whether an interest in a VIE makes the holder the primary beneficiary of the VIE. ASU 2009-17 is effective for interim and annual reporting periods beginning after November 15, 2009. Our adoption of ASU 2009-17 did not have a material impact on our consolidated financial statements.

(2) INVESTMENTS

At December 31, 2009, short-term investments were $30.0 million, which consisted of U.S. government obligations with maturities of greater than 90 days. These investments were redeemed during the six months ended June 30, 2010.

(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 translation adjustments related to long-term intercompany loans, make up the translation adjustment in other comprehensive income.

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

	Three-Months Ended June 30,		Six-Months Ended June 30,	
Diluted earnings (loss) per share	**2010**	**2009**	**2010**	**2009**
Net earnings (loss)	$ 40,317	$ (6,626)	$ 96,440	$ 726
Unrealized gain on marketable securities, net of tax	0	10,234	0	8,151
Income (loss) on foreign currency translation adjustment, net of tax	(6,120)	6,881	(10,350)	3,899
Comprehensive income	34,197	10,489	86,090	12,776
Comprehensive income (loss) attributable to noncontrolling interest	(107)	(654)	28	(1,542)
Comprehensive income attributable to parent	$ 34,090	$ 11,143	$ 86,118	$ 14,318

Table of Contents

(5) STOCK COMPENSATION

The Company recognizes compensation expense for stock-based awards based on the grant date fair value. Stock compensation expense was $3.4 million and $0.6 million for the three months ended June 30, 2010 and 2009, respectively. Stock compensation expense was $6.7 million and $1.2 million for the six months ended June 30, 2010 and 2009, respectively.

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

	SHARES	WEIGHTED AVERAGE EXERCISE PRICE	WEIGHTED AVERAGE REMAINING CONTRACTUAL TERM	AGGREGATE INTRINSIC VALUE
Outstanding at December 31, 2009	1,505,694	$ 12.01		
Granted	0	0		
Exercised	(838,283)	12.56		
Cancelled	(24,791)	3.94		
Outstanding at June 30, 2010	642,620	11.61	1.9 years	$16,008,636
Exercisable at June 30, 2010	642,620	11.61	1.9 years	$16,008,636

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, 2010 is presented below:

	SHARES	WEIGHTED AVERAGE GRANT-DATE FAIR VALUE
Nonvested at December 31, 2009	2,158,644	$ 17.86
Granted	129,000	30.96
Vested	(102,644)	17.06
Cancelled	0	0
Nonvested at June 30, 2010	2,185,000	18.67

As of June 30, 2010, there was $31.5 million of unrecognized compensation cost related to nonvested common shares. The cost is expected to be amortized over a weighted average period of 2.3 years.

(6) EARNINGS 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 represents the weighted average number of common shares and potential common shares, if dilutive, that would arise from the exercise of stock options and nonvested shares using the treasury stock method.

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):

Basic earnings (loss) per share	**Three-Months Ended June 30,**		**Six-Months Ended June 30,**	
	2010	**2009**	**2010**	**2009**
Net earnings (loss) attributable to Skechers U.S.A., Inc.	$40,237	$ (5,927)	$96,533	$ 2,293
Weighted average common shares outstanding	47,422	46,282	47,107	46,252
Basic earnings (loss) per share attributable to Skechers U.S.A., Inc.	$ 0.85	$ (0.13)	$ 2.05	$ 0.05

Table of Contents

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	**2010**	**2009**	**2010**	**2009**
Net earnings (loss) attributable to Skechers U.S.A., Inc.	$ 40,237	$ (5,927)	$ 96,533	$ 2,293
Weighted average common shares outstanding	47,422	46,282	47,107	46,252
Dilutive effect of stock options	1,708	0	1,848	172
Weighted average common shares outstanding	49,130	46,282	48,955	46,424