APPLIED INDUSTRIAL TECHNOLOGIES INC
Form 10-Q
May 05, 2014
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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended MARCH 31, 2014

OR

o 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 1-2299

APPLIED INDUSTRIAL TECHNOLOGIES, INC.
(Exact name of registrant as specified in its charter)

Ohio	34-0117420
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
One Applied Plaza, Cleveland, Ohio	44115
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (216) 426-4000
(Former name, former address and former fiscal year, if changed since last report)

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 x 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 x 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 the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	x	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 x

There were 41,771,644 (no par value) shares of common stock outstanding on April 15, 2014.

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PART I: FINANCIAL INFORMATION

ITEM I: FINANCIAL STATEMENTS

APPLIED INDUSTRIAL TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED STATEMENTS OF CONSOLIDATED INCOME
(Unaudited)
(In thousands, except per share amounts)

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2014	2013	2014	2013
Net Sales	$618,006	$621,654	$1,805,260	$1,821,690
Cost of Sales	446,786	447,254	1,300,862	1,319,838
Gross Profit	171,220	174,400	504,398	501,852
Selling, Distribution and Administrative, including depreciation	131,047	130,923	384,849	373,488
Operating Income	40,173	43,477	119,549	128,364
Interest (Income) Expense, net	(11)	107	(102)	147
Other (Income) Expense, net	(388)	(1,027)	(1,749)	(1,913)
Income Before Income Taxes	40,572	44,397	121,400	130,130
Income Tax Expense	10,178	15,095	38,253	44,253
Net Income	$30,394	$29,302	$83,147	$85,877
Net Income Per Share - Basic	$0.73	$0.70	$1.98	$2.04
Net Income Per Share - Diluted	$0.72	$0.69	$1.96	$2.02
Cash dividends per common share	$0.25	$0.23	$0.71	$0.65
Weighted average common shares outstanding for basic computation	41,880	42,098	42,039	42,038
Dilutive effect of potential common shares	362	472	399	479
Weighted average common shares outstanding for diluted computation	42,242	42,570	42,438	42,517

See notes to condensed consolidated financial statements.

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APPLIED INDUSTRIAL TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED STATEMENTS OF CONSOLIDATED COMPREHENSIVE INCOME
(Unaudited)
(In thousands)

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2014	2013	2014	2013
Net income per the condensed statements of consolidated income	$30,394	$29,302	$83,147	$85,877
Other comprehensive income (loss), before tax:				
Foreign currency translation adjustments	(3,876)	(5,466)	(10,736)	2,941
Postemployment benefits:				
Reclassification of actuarial losses and prior service cost into SD&A expense and included in net periodic pension costs	96	218	287	654
Unrealized gain (loss) on investment securities available for sale	49	42	148	65
Total of other comprehensive income (loss), before tax	(3,731)	(5,206)	(10,301)	3,660
Income tax expense related to items of other comprehensive income	53	99	162	278
Other comprehensive income (loss), net of tax	(3,784)	(5,305)	(10,463)	3,382
Comprehensive income, net of tax	$26,610	$23,997	$72,684	$89,259

See notes to condensed consolidated financial statements.

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APPLIED INDUSTRIAL TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(In thousands)

	March 31, 2014	June 30, 2013
ASSETS		
Current assets		
Cash and cash equivalents	$69,086	$73,164
Accounts receivable, less allowances of $8,479 and $7,737	344,096	329,880
Inventories	320,045	281,417
Other current assets	41,284	52,819
Total current assets	774,511	737,280
Property, less accumulated depreciation of $157,454 and $157,506	78,834	83,243
Intangibles, net	88,368	91,267
Goodwill	111,201	106,849
Deferred tax assets	23,792	21,026
Other assets	19,945	19,041
TOTAL ASSETS	$1,096,651	$1,058,706
LIABILITIES AND SHAREHOLDERS’ EQUITY		
Current liabilities		
Accounts payable	$145,352	$136,575
Short-term debt	30,000	—
Compensation and related benefits	46,849	63,899
Other current liabilities	46,022	45,426
Total current liabilities	268,223	245,900
Postemployment benefits	25,197	30,919
Other liabilities	22,159	22,272
TOTAL LIABILITIES	315,579	299,091
Shareholders’ Equity		
Preferred stock—no par value; 2,500 shares authorized; none issued or outstanding		
Common stock—no par value; 80,000 shares authorized; 54,213 shares issued	10,000	10,000
Additional paid-in capital	156,495	153,893
Income retained for use in the business	877,547	824,362
Treasury shares—at cost (12,396 and 12,044 shares)	(249,086)	(225,219)
Accumulated other comprehensive income (loss)	(13,884)	(3,421)
TOTAL SHAREHOLDERS’ EQUITY	781,072	759,615
TOTAL LIABILITIES AND SHAREHOLDERS’ EQUITY	$1,096,651	$1,058,706

See notes to condensed consolidated financial statements.

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APPLIED INDUSTRIAL TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED STATEMENTS OF CONSOLIDATED CASH FLOWS
(Unaudited)
(In thousands)

	Nine Months Ended March 31,	
	2014	2013
Cash Flows from Operating Activities		
Net income	$83,147	$85,877
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of property	10,119	9,234
Amortization of intangibles	9,518	9,716
Unrealized foreign exchange transactions loss (gain)	136	(624)
Amortization of stock options and appreciation rights	1,703	1,959
Loss (gain) on sale of property	37	(223)
Other share-based compensation expense	2,946	2,873
Changes in operating assets and liabilities, net of acquisitions	(60,451)	(39,787)
Other, net	(2,829)	31
Net Cash provided by Operating Activities	44,326	69,056
Cash Flows from Investing Activities		
Property purchases	(6,492)	(9,836)
Proceeds from property sales	348	737
Net cash paid for acquisition of businesses, net of cash acquired	(17,000)	(67,591)
Net Cash used in Investing Activities	(23,144)	(76,690)
Cash Flows from Financing Activities		
Borrowings under revolving credit facility	30,000	—
Purchases of treasury shares	(23,992)	—
Dividends paid	(29,961)	(27,468)
Excess tax benefits from share-based compensation	2,525	1,718
Acquisition holdback payments	(1,824)	(3,576)
Exercise of stock options and appreciation rights	95	498
Net Cash used in Financing Activities	(23,157)	(28,828)
Effect of Exchange Rate Changes on Cash	(2,103)	1,103
Decrease in Cash and Cash Equivalents	(4,078)	(35,359)
Cash and Cash Equivalents at Beginning of Period	73,164	78,442
Cash and Cash Equivalents at End of Period	$69,086	$43,083

See notes to condensed consolidated financial statements.

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APPLIED INDUSTRIAL TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Amounts in thousands, except per share amounts) (Unaudited)

1. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of the financial position of Applied Industrial Technologies, Inc. (the “Company”, or “Applied”) as of March 31, 2014, and the results of its operations for the three and nine month periods ended March 31, 2014 and 2013 and its cash flows for the nine months ended March 31, 2014 and 2013, have been included. The condensed consolidated balance sheet as of June 30, 2013 has been derived from the audited consolidated financial statements at that date. This Quarterly Report on Form 10-Q should be read in conjunction with the Company’s Annual Report on Form 10-K for the year ended June 30, 2013.

Operating results for the three and nine month periods ended March 31, 2014 are not necessarily indicative of the results that may be expected for the remainder of the fiscal year ending June 30, 2014.

Change in Accounting Principle - Alignment of Canadian Subsidiary Reporting
Effective July 1, 2013, the Company aligned the consolidation of the Company’s Canadian subsidiary in the consolidated financial statements which previously included results on a one month reporting lag. The Company believes that this change in accounting principle is preferable as it provides contemporaneous reporting within our consolidated financial statements. In accordance with applicable accounting literature, the elimination of a one month reporting lag of a subsidiary is treated as a change in accounting principle and requires retrospective application. The Company has determined that the effect of this change is not material to the financial statements for all periods presented and therefore, the Company has not presented retrospective application of this change. The net impact of the lag elimination of $1,200 of income for the month of June 2013 has been included within “Other (Income) Expense, net” on the Statement of Consolidated Income for the nine months ended March 31, 2014. The three months ended March 31, 2014 reflect the same results, had the financial statements been retrospectively adjusted. The nine months ended March 31, 2014 reflect the same results, had the financial statements been retrospectively adjusted, with the exception of net income which would have decreased $1,200. Net sales, operating income and net income for the three months ended March 31, 2013, would have increased by $3,500, $800 and $700 respectively had the financial statements been retrospectively adjusted. Net sales, operating income and net income for the nine months ended March 31, 2013, would have increased by $500 and decreased by $400 and $400 respectively had the financial statements been retrospectively adjusted.

Change in Accounting Principle - Alignment of Mexican Subsidiary Reporting
Effective January 1, 2014, the Company aligned the consolidation of the Company’s Mexican subsidiary in the consolidated financial statements which previously included results on a one month reporting lag. The Company believes that this change in accounting principle is preferable as it provides contemporaneous reporting within our consolidated financial statements. In accordance with applicable accounting literature, the elimination of a one month reporting lag of a subsidiary is treated as a change in accounting principle and requires retrospective application. The Company has determined that the effect of this change is not material to the financial statements for all periods presented and therefore, the Company has not presented retrospective application of this change. The net impact of the lag elimination of $200 of income for the month of December 2013 has been included within “Other (Income) Expense, net” on the Statement of Consolidated Income for the three and nine months ended March 31, 2014. The three months ended March 31, 2014 reflect the same results, had the financial statements been retrospectively adjusted, with

the exception of net income which would have decreased $200. Net sales, operating income and net income for the nine months ended March 31, 2014 would have decreased by $1,100, $100 and $300 had the financial statements been retrospectively adjusted. Net sales, operating income and net income for the three months ended March 31, 2013, would have increased by $800, and decreased by $200 and $300 respectively had the financial statements been retrospectively adjusted. Net sales, operating income and net income for the nine months ended March 31, 2013, would have decreased by $1,000, $600 and $500 respectively had the financial statements been retrospectively adjusted.

APPLIED INDUSTRIAL TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Amounts in thousands, except per share amounts) (Unaudited)

Impact of Changes in Accounting Principle - Alignment of Subsidiary Reporting
The Company has determined that the effect of both the Canadian and Mexican reporting lag eliminations is not material to the financial statements for all periods presented and therefore, the Company has not presented retrospective application of these changes. All subsidiary reporting is now aligned with that of the consolidated financial statements.
Inventory

The Company uses the last-in, first-out (LIFO) method of valuing U.S. inventories. An actual valuation of inventory under the LIFO method can be made only at the end of each year based on the inventory levels and costs at that time. Accordingly, interim LIFO calculations are based on management's estimates of expected year-end inventory levels and costs and are subject to the final year-end LIFO inventory determination.

Reclassifications

Certain reclassifications have been made to the prior year financial statements to conform to the 2014 presentation.

2. BUSINESS COMBINATION

In December 2013, the Company acquired substantially all of the net assets of Texas Oilpatch Services Corporation, a Texas distributor of bearings, oil seals, power transmission products, and related replacement parts to the oilfield industry. The acquired business is included in the Service Center Based Distribution segment from December 31, 2013.

The results of operations for this acquisition are not material for any period presented.

3. GOODWILL AND INTANGIBLES

The changes in the carrying amount of goodwill for both the Service Center Based Distribution segment and the Fluid Power Businesses segment for the nine month period ended March 31, 2014 are as follows:

	Service Centers	Fluid Power	Total
Balance at July 1, 2013	$105,920	$929	$106,849
Goodwill acquired during the period	5,727		5,727
Other, primarily currency translation	(1,375)		(1,375)
Balance at March 31, 2014	$110,272	$929	$111,201

At March 31, 2014, accumulated goodwill impairment losses, subsequent to fiscal year 2002, totaled $36,605 and related to the Fluid Power Businesses segment.

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APPLIED INDUSTRIAL TECHNOLOGIES, INC. AND SUBSIDIARIES
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(Amounts in thousands, except per share amounts) (Unaudited)

The Company’s identifiable intangible assets resulting from business combinations are amortized over their estimated period of benefit and consist of the following:

March 31, 2014	Amount	Accumulated Amortization	Net Book Value
Finite-Lived Intangibles:			
Customer relationships	$106,173	$44,496	$61,677
Trade names	26,314	9,755	16,559
Vendor relationships	15,365	6,292	9,073
Non-competition agreements	2,204	1,145	1,059
Total Intangibles	$150,056	$61,688	$88,368

June 30, 2013	Amount	Accumulated Amortization	Net Book Value
Finite-Lived Intangibles:			
Customer relationships	$100,854	$38,844	$62,010
Trade names	26,690	8,643	18,047
Vendor relationships	15,433	5,443	9,990
Non-competition agreements	4,743	3,523	1,220
Total Intangibles	$147,720	$56,453	$91,267

Amounts include the impact of foreign currency translation. Fully amortized amounts are written off.

During the nine month period ended March 31, 2014, the Company acquired identifiable intangible assets with a preliminary acquisition cost allocation and weighted-average life as follows:

	Acquisition Cost Allocation	Weighted-Average Life
Customer relationships	$6,940	20 years
Trade names	160	5 years
Non-competition agreements	310	5 years
Total Intangibles Acquired	$7,410	19 years

Estimated future amortization expense by fiscal year (based on the Company’s identifiable intangible assets as of March 31, 2014) for the next five years is as follows: $3,200 for the remainder of 2014, $12,100 for 2015, $11,000 for 2016, $10,300 for 2017, $9,000 for 2018 and $8,000 for 2019.

4. FAIR VALUE MEASUREMENTS

Marketable securities measured at fair value at March 31, 2014 and June 30, 2013 totaled $10,719 and $10,483, respectively. These marketable securities are held in a rabbi trust for a non-qualified deferred compensation plan. The marketable securities are included in Other Assets on the accompanying condensed consolidated balance sheets and their fair values were based upon quoted market prices in an active market (Level 1 in the fair value hierarchy).

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5. SHAREHOLDERS' EQUITY

Accumulated Other Comprehensive Income (Loss)

Changes in the accumulated other comprehensive income (loss), are comprised of the following:

	Three Months Ended March 31, 2014			
	Foreign currency translation adjustment	Unrealized gain (loss) on securities available for sale	Postemployment benefits	Total Accumulated other comprehensive income (loss)
Balance at December 31, 2013	$(6,500)	$13	$(3,613)	$(10,100)
Other comprehensive income (loss)	(3,876)	33		(3,843)
Amounts reclassified from accumulated other comprehensive income (loss)	—		59	59
Net current-period other comprehensive income (loss), net of taxes	(3,876)	33	59	(3,784)
Balance at March 31, 2014	$(10,376)	$46	$(3,554)	$(13,884)

	Nine Months Ended March 31, 2014			
	Foreign currency translation adjustment	Unrealized gain (loss) on securities available for sale	Postemployment benefits	Total Accumulated other comprehensive income (loss)
Balance at July 1, 2013	$360	$(52)	$(3,729)	$(3,421)
Other comprehensive income (loss)	(10,736)	98		(10,638)
Amounts reclassified from accumulated other comprehensive income (loss)			175	175
Net current-period other comprehensive income (loss), net of taxes	(10,736)	98	175	(10,463)
Balance at March 31, 2014	$(10,376)	$46	$(3,554)	$(13,884)

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Other Comprehensive Income (Loss)

Details of other comprehensive income (loss) are as follows:

	Three Months Ended March 31,					
	2014			2013		
	Pre-Tax Amount	Tax Expense (Benefit)	Net Amount	Pre-Tax Amount	Tax Expense (Benefit)	Net Amount
Foreign currency translation adjustments	$(3,876)	$—	$(3,876)	$(5,466)	$—	$(5,466)
Postemployment benefits:						
Reclassification of actuarial losses and prior service cost into SD&A expense and included in net periodic pension costs	96	37	59	218	85	133
Unrealized gain (loss) on investment securities available for sale	49	16	33	42	14	28
Other comprehensive income (loss)	$(3,731)	$53	$(3,784)	$(5,206)	$99	$(5,305)

	Nine Months Ended March 31,					
	2014			2013		
	Pre-Tax Amount	Tax Expense (Benefit)	Net Amount	Pre-Tax Amount	Tax Expense (Benefit)	Net Amount
Foreign currency translation adjustments	$(10,736)	$—	$(10,736)	$2,941	$—	$2,941
Postemployment benefits:						
Reclassification of actuarial losses and prior service cost into SD&A expense and included in net periodic pension costs	287	112	175	654	255	399
Unrealized gain (loss) on investment securities available for sale	148	50	98	65	23	42
Other comprehensive income (loss)	$(10,301)	$162	$(10,463)	$3,660	$278	$3,382

Antidilutive Common Stock Equivalents

In the three and nine month periods ended March 31, 2014 and 2013, respectively, stock options and stock appreciation rights related to the acquisition of 306 and 180 shares of common stock in the three month periods and 306 and 208 shares of common stock in the nine month periods were not included in the computation of diluted earnings per share for the periods then ended as they were anti-dilutive.

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(Amounts in thousands, except per share amounts) (Unaudited)

6. BENEFIT PLANS

The following table provides summary disclosures of the net periodic postemployment costs recognized for the Company's postemployment benefit plans:

	Pension Benefits		Retiree Health Care Benefits	
Three Months Ended March 31,	2014	2013	2014	2013
Components of net periodic cost:				
Service cost	$19	$20	$12	$20
Interest cost	295	314	35	47
Expected return on plan assets	(104)	(101)		
Recognized net actuarial loss (gain)	153	184	(9)	(13)
Amortization of prior service cost	20	21	(68)	27
Net periodic cost	$383	$438	$(30)	$81

	Pension Benefits		Retiree Health Care Benefits	
Nine Months Ended March 31,	2014	2013	2014	2013
Components of net periodic cost:				
Service cost	$57	$60	$36	$60
Interest cost	885	945	104	142
Expected return on plan assets	(312)	(303)		
Recognized net actuarial loss (gain)	459	551	(28)	(40)
Amortization of prior service cost	59	62	(203)	80
Net periodic cost	$1,148	$1,315	$(91)	$242

The Company contributed $6,492 to its pension benefit plans and $165 to its retiree health care plans in the nine months ended March 31, 2014. Expected contributions for the remainder of fiscal 2014 are $200 for the pension benefit plans to fund scheduled retirement payments and $85 for retiree health care plans.

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APPLIED INDUSTRIAL TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Amounts in thousands, except per share amounts) (Unaudited)

7. SEGMENT AND GEOGRAPHIC INFORMATION

The accounting policies of the Company's reportable segments are generally the same as those used to prepare the condensed consolidated financial statements. Intercompany sales primarily from the Fluid Power Businesses segment to the Service Center Based Distribution segment of $5,369 and $5,889, in the three months ended March 31, 2014 and 2013, respectively, and $16,564 and $14,618 in the nine months ended March 31, 2014 and 2013, respectively, have been eliminated in the Segment Financial Information tables below.

Three Months Ended	Service Center Based Distribution	Fluid Power Businesses	Total
March 31, 2014			
Net sales	$492,678	$125,328	$618,006
Operating income for reportable segments	28,754	13,442	42,196
Depreciation and amortization of property	2,964	363	3,327
Capital expenditures	2,021	345	2,366
March 31, 2013			
Net sales	$506,727	$114,927	$621,654
Operating income for reportable segments	35,357	9,607	44,964
Depreciation and amortization of property	2,735	463	3,198
Capital expenditures	2,894	99	2,993

Nine Months Ended	Service Center Based Distribution	Fluid Power Businesses	Total
March 31, 2014			
Net sales	$1,450,705	$354,555	$1,805,260
Operating income for reportable segments	82,695	33,263	115,958
Assets used in business	879,349	217,302	1,096,651
Depreciation and amortization of property	8,951	1,168	10,119
Capital expenditures	5,755	737	6,492
March 31, 2013			
Net sales	$1,485,029	$336,661	$1,821,690
Operating income for reportable segments	97,445	28,758	126,203
Assets used in business	833,211	202,726	1,035,937
Depreciation and amortization of property	7,864	1,370	9,234
Capital expenditures	9,488	348	9,836

Enterprise Resource Planning system (ERP) related assets are included in assets used in business and capital expenditures within the Service Center Based Distribution segment. Expenses associated with the ERP are included in Corporate and other expense (income) net, line in the reconciliation of operating income for reportable segments to the consolidated income before income taxes table below.

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APPLIED INDUSTRIAL TECHNOLOGIES, INC. AND SUBSIDIARIES
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(Amounts in thousands, except per share amounts) (Unaudited)

A reconciliation of operating income for reportable segments to the condensed consolidated income before income taxes is as follows:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2014	2013	2014	2013
Operating income for reportable segments	$42,196	$44,964	$115,958	$126,203
Adjustment for:				
Intangible amortization—Service Center Based Distribution	1,102	1,637	4,484	4,164
Intangible amortization—Fluid Power Businesses	2,086	1,873	5,034	5,553
Corporate and other expense (income), net	(1,165)	(2,023)	(13,109)	(11,878)
Total operating income	40,173	43,477	119,549	128,364
Interest (income) expense, net	(11)	107	(102)	147
Other (income) expense, net	(388)	(1,027)	(1,749)	(1,913)
Income before income taxes	$40,572	$44,397	$121,400	$130,130

The change in corporate and other expense (income), net is due to changes in the amounts and levels of expenses being allocated to the segments. The expenses being allocated include corporate charges for working capital, logistics support and other items.

Net sales are presented in geographic areas based on the location of the facility shipping the product and are as follows:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2014	2013	2014	2013
Geographic Areas:				
United States	$519,713	$514,941	$1,500,252	$1,492,795
Canada	64,922	70,497	202,439	218,848
Other countries	33,371	36,216	102,569	110,047
Total	$618,006	$621,654	$1,805,260	$1,821,690

Other countries consisted of Mexico, Australia and New Zealand.

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(Amounts in thousands, except per share amounts) (Unaudited)

8. OTHER (INCOME) EXPENSE , NET

Other (income) expense, net consists of the following:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2014	2013	2014	2013
Unrealized (gain) loss on assets held in rabbi trust for a nonqualified deferred compensation plan	$(110)	$(602)	$(1,355)	$(1,183)
Elimination of one-month Canadian and Mexican reporting lag, effective July 1, 2013 and January 1, 2014, respectively	(175)	—	(1,342)	—
Foreign currency transactions (gain) loss	46	(231)	953	(656)
Other, net	(149)	(194)	(5)	(74)
Total other (income) expense, net	$(388)	$(1,027)	$(1,749)	$(1,913)

9. INCOME TAXES

The effective tax rates for the three and nine month periods ended March 31, 2014 were lower than the comparable prior year periods primarily due to the reversal of the deferred tax liability associated with undistributed earnings in Canada, as well as the reversal of tax reserves associated with certain uncertain tax positions.

During the three month period ended March 31, 2014, the Company reversed a $2,800 deferred tax liability related to a portion of the undistributed earnings in Canada. The liability was reversed as it was determined that all undistributed earnings in Canada would be permanently reinvested. Additionally, $1,100 of tax reserves were reversed due to the expiration of certain statutes of limitations for U.S. tax audits, during the three months ended March 31, 2014.

10. SUBSEQUENT EVENTS

On May 1, 2014, the Company acquired Reliance Industrial Products, headquartered in Nisku, Alberta, Canada, with operations in Western Canada and the Western United States, for a total purchase price in the amount of $189,800. This business will expand Applied's global capabilities within the oil and gas industry and will be a part of the Service Center Based Distribution segment. The Company funded the acquisition by using available cash in Canada in the amount of $31,900, existing revolving credit facilities of $36,600 and a new $100,000 five year term loan facility, with the remainder to be paid to the sellers over the next several years. The results of operations acquired will be included in the Company's results of operations from May 1, 2014.

APPLIED INDUSTRIAL TECHNOLOGIES, INC. AND SUBSIDIARIES
REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The accompanying condensed consolidated financial statements of the Company have been reviewed by the Company's independent registered public accounting firm, Deloitte & Touche LLP, whose report covering their reviews of the condensed consolidated financial statements follows.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of
Applied Industrial Technologies, Inc.
Cleveland, Ohio

We have reviewed the accompanying condensed consolidated balance sheet of Applied Industrial Technologies, Inc. and subsidiaries (the "Company") as of March 31, 2014, and the related condensed statements of consolidated income and condensed consolidated comprehensive income for the three-month and nine-month periods ended March 31, 2014 and 2013, and of condensed consolidated cash flows for the nine-month periods ended March 31, 2014 and 2013. These interim financial statements are the responsibility of the Company's management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to such condensed consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of the Company as of June 30, 2013, and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for the year then ended (not presented herein); and in our report dated August 20, 2013, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of June 30, 2013 is fairly stated, in all material respects, in relation to the consolidated balance sheet fr