

NATCO GROUP INC
Form 10-Q
May 10, 2006
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2006

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 1-15603

NATCO Group Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of

incorporation or organization)

2950 North Loop West

7th Floor

22-2906892
(I.R.S. Employer

Identification No.)

77092

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Houston, Texas
(Address of principal executive offices)

713-683-9292

(Zip Code)

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

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

As of April 28, 2006, the issuer had outstanding 17,016,088 shares of common stock, par value \$0.01 per share.

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NATCO GROUP INC.

FORM 10-Q

For the Quarter Ended March 31, 2006

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Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements****NATCO GROUP INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS**

(in thousands, except share and par value data)

	March 31, 2006 (unaudited)	December 31, 2005
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 13,602	\$ 9,198
Trade accounts receivable, less allowance for doubtful accounts of \$1,397 and \$1,123 as of March 31, 2006 and December 31, 2005, respectively	116,304	111,770
Inventories	44,211	37,194
Deferred income tax assets, net	3,462	3,465
Prepaid expenses and other current assets	3,324	3,612
Total current assets	180,903	165,239
Property, plant and equipment, net	32,851	33,263
Goodwill, net	80,882	80,891
Deferred income tax assets, net	3,395	3,329
Other assets, net	1,596	1,021
Total assets	\$ 299,627	\$ 283,743

LIABILITIES, REDEEMABLE CONVERTIBLE PREFERRED STOCK AND**STOCKHOLDERS EQUITY**

Current liabilities:		
Trade accounts payable and other	\$ 42,628	\$ 48,720
Accrued expenses and other	43,708	41,781
Customer advanced billings and payments	29,387	18,272
Current portion of long-term debt	24,393	6,429
Income taxes payable	3,678	890
Total current liabilities	143,794	116,092
Long-term debt, excluding current installments		20,964
Long-term deferred tax liabilities	683	483
Postretirement benefits and other long-term liabilities	9,683	9,814
Total liabilities	154,160	147,353
Commitments and contingencies		
Series B redeemable convertible preferred stock (aggregate redemption value of \$15,000), \$.01 par value. 15,000 shares authorized, issued and outstanding (net of issuance costs)	14,222	14,222
Stockholders equity:		

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Preferred stock, \$.01 par value. Authorized 5,000,000 shares (of which 500,000 are designated as Series A and 15,000 are designated as Series B); no shares issued and outstanding (except Series B shares above)		
Series A preferred stock, \$.01 par value. Authorized 500,000 shares; no shares issued and outstanding		
Common stock, \$.01 par value. Authorized 50,000,000 shares; issued and outstanding 16,995,238 and 16,914,052 shares as of March 31, 2006 and December 31, 2005, respectively	170	169
Additional paid-in-capital	103,197	101,671
Accumulated retained earnings	27,398	19,914
Treasury stock, no shares and 2,550 shares at cost as of March 31, 2006 and December 31, 2005, respectively		(22)
Accumulated other comprehensive income	480	436
 Total stockholders' equity	 131,245	 122,168
 Total liabilities, redeemable convertible preferred stock and stockholders' equity	 \$ 299,627	 \$ 283,743

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents**NATCO GROUP INC. AND SUBSIDIARIES****UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(in thousands, except per share data)**

	Three Months Ended	
	March 31, 2006	2005
Revenues:		
Products	\$ 97,006	\$ 71,735
Services	20,761	16,921
Total revenues	\$ 117,767	\$ 88,656
Cost of goods sold and services:		
Products	\$ 75,935	\$ 58,425
Services	10,424	8,946
Total cost of goods sold and services	\$ 86,359	\$ 67,371
Gross profit	\$ 31,408	\$ 21,285
Selling, general and administrative expense	16,994	14,190
Depreciation and amortization expense	1,445	1,323
Closure, severance and other	50	42
Interest expense	703	1,015
Interest cost on postretirement benefit liability	50	210
Interest income	(63)	(52)
Other, net	(447)	(80)
Income before income taxes	\$ 12,676	\$ 4,637
Income tax provision	4,817	1,762
Net income	\$ 7,859	\$ 2,875
Preferred stock dividends	375	375
Net income allocable to common stockholders	\$ 7,484	\$ 2,500
Earnings per share basic:		
Net income	\$ 0.45	\$ 0.16
Earnings per share diluted:		
Net income	\$ 0.41	\$ 0.16
Basic weighted average number of shares of common stock outstanding	16,663	15,816
Diluted weighted average number of shares of common stock outstanding	19,046	16,042

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents**NATCO GROUP INC. AND SUBSIDIARIES****UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in thousands)

	Three Months Ended	
	2006	March 31, 2005 ⁽¹⁾
Cash flows from operating activities:		
Net income	\$ 7,859	\$ 2,875
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Deferred income tax benefit	120	359
Depreciation and amortization expense	1,445	1,323
Non-cash interest expense	86	140
Stock compensation expense	613	119
Tax benefit of stock options exercised	73	222
Revaluation of warrants		204
Interest cost on postretirement benefit liability	50	210
Net payments on postretirement benefit liability	(234)	(388)
Loss (gain) on the sale of property, plant and equipment	45	(388)
Change in assets and liabilities:		
Increase in trade accounts receivable	(3,661)	(4,665)
(Increase) decrease in inventories	(6,986)	1,189
Decrease (increase) in prepaid expense and other current assets	212	(2)
Decrease (increase) in long-term assets	(625)	(12)
Decrease in accounts payable	(7,199)	(2,224)
Increase in accrued expenses and other	1,624	1,454
Increase in income tax payable	2,812	
Increase in customer advanced billings and payments	11,149	658
Net cash provided by operating activities	7,383	1,074
Cash flows from investing activities:		
Capital expenditures for property, plant and equipment	(962)	(880)
Investment in other long-term intangible asset	(375)	
Proceeds from the sale of property, plant and equipment	9	962
Net cash (used in) provided by investing activities	(1,328)	82
Cash flows from financing activities:		
Repayments of long-term debt	(3,000)	(1,631)
Borrowings of long-term debt		889
Proceeds from the stock issuances related to stock options, net	534	1,554
Tax benefit of stock options exercised	327	
Change in bank overdrafts	454	(2,794)
Deferred financing fees		(105)
Net cash used in financing activities	(1,685)	(2,087)
Effect of exchange rate changes on cash and cash equivalents	34	25
Increase (decrease) in cash and cash equivalents	4,404	(906)

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Cash and cash equivalents at beginning of period	9,198	2,194
Cash and cash equivalents at end of period	\$ 13,602	\$ 1,288
Cash payments for:		
Interest	\$ 579	\$ 685
Income taxes	\$ 1,413	\$ 1,388

⁽¹⁾ The line Net payments on postretirement benefit liability has been reclassified from cash flows from financing activities to cash flows from operating activities for period presented. Net cash used in investing activities and Increase (decrease) in cash and cash equivalents in total were unaffected from this reclassification. Refer to Note 1, Basis of Presentation and Reclassifications in the accompanying Notes to Unaudited Condensed Consolidated Financial Statements for further information.

See accompanying notes to unaudited condensed consolidated financial statements.

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NATCO GROUP INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(1) Basis of Presentation and Reclassifications

Basis of Presentation

The accompanying condensed consolidated interim financial statements and related disclosures are unaudited and have been prepared by NATCO Group Inc. pursuant to accounting principles generally accepted in the United States of America (US GAAP) for interim consolidated financial statements and the rules and regulations of the United States Securities and Exchange Commission. As permitted by these regulations, certain information and footnote disclosures that would typically be required in financial statements prepared in accordance with US GAAP have been condensed or omitted. However, the Company's management believes that these statements reflect all the normal recurring adjustments necessary for a fair presentation, in all material respects, of the results of operations for the periods presented, so that these interim financial statements are not misleading. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K filing for the year ended December 31, 2005.

To prepare financial statements in accordance with generally accepted accounting principles, the Company's management is required 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 reported amounts of revenues and expenses incurred during the reporting period. Actual results could differ from those estimates.

References to NATCO and the Company are used throughout this document and relate collectively to NATCO Group Inc. and its consolidated subsidiaries.

Reclassifications

Certain reclassifications have been made to the fiscal year 2005 amounts in order to present these results on a comparable basis with amounts for fiscal year 2006. These reclassifications had no effect on net income.

The Company's previous accounting policy was to classify cash flows from its net postretirement benefit liability as a financing activity in our consolidated statements of cash flows because the retirees covered were never employed by the Company and the decision to assume the obligation was a financing determination made at the time of the 1989 acquisition of National Tank Company and W.S. Tyler, Inc. The estimated postretirement liability directly impacted the purchase price for these assets and also impacted the overall financing consideration and structure of the transaction.

Paragraph 18 of the Statement of Financial Accounting Standards (SFAS) No. 95 states financing activities include obtaining resources from owners and providing them with a return on, and a return of, their investment; borrowing money and repaying amounts borrowed, or otherwise settling the obligation; and obtaining and paying for other resources obtained from creditors on long-term credit and paragraph 21 of SFAS No. 95 states Operating activities include all transactions and other events that are not defined as investing or financing activities. Since, the lines Net payments on postretirement benefit liability on the Company's unaudited condensed consolidated statement of cash flow are not included in the scope of what is defined as financing activities in paragraph 18 of SFAS No. 95, the Company therefore believes the lines Net payments on postretirement benefit liability on our unaudited condensed consolidated statement of cash flow relate to operating activities of the Company rather than financing activities as previously reported. The Company has amended the unaudited condensed consolidated statement of cash flow included in this report to be in accordance with SFAS No. 95.

Table of Contents**NATCO GROUP INC. AND SUBSIDIARIES****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

For the quarter ended March 31, 2005, the Company reclassified the postretirement payments and receipts as operating activities from financing activities in the unaudited consolidated statement of cash flow. For the quarter ended March 31, 2005, this reclassification had the effect of reducing net cash provided by operating activities of \$388,000 and increasing net cash used in financing activities by \$388,000 for the quarter ended March 31, 2005 from that previously reported. This reclassification does not impact the unaudited condensed consolidated statement of operation or the Net cash used in investing activities and Increases (decreases) in cash and cash equivalents in total on the unaudited condensed consolidated statement of cash flow.

(2) Inventories

Inventories consisted of the following amounts:

	March 31,	December 31,
	2006	2005
	(unaudited)	
	(in thousands)	
Finished goods	\$ 10,606	\$ 9,670
Work-in-process	19,957	15,138
Raw materials and supplies	19,537	17,180
Inventories at FIFO and weighted average	50,100	41,988
Excess of FIFO over LIFO cost	(5,889)	(4,794)