SIFCO INDUSTRIES INC
Form 10-Q
August 11, 2008

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

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

For the quarterly period ended June 30, 2008

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 1-5978

SIFCO Industries, Inc.

(Exact name of registrant as specified in its charter)

Ohio	34-0553950
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
970 East 64th Street, Cleveland Ohio	44103
(Address of principal executive offices)	(Zip Code)

(216) 881-8600

(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 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. (Check one):

Large Accelerated Filer o	Accelerated Filer o	Non-accelerated Filer o	Smaller reporting company þ
		(Do not check if a 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 o No þ

The number of the Registrant s Common Shares outstanding at June 30, 2008 was 5,293,966.

TABLE OF CONTENTS

Table of Contents

Part I. Financial Information
Item 1. Financial Statements

SIFCO Industries, Inc. and Subsidiaries
Consolidated Condensed Statements of Operations
(Unaudited)
(Amounts in thousands, except per share data)

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2008	**2007**	**2008**	**2007**
Net sales	**$ 27,333**	$ 24,022	**$ 76,493**	$ 64,678
Operating expenses:				
Cost of goods sold	**20,977**	18,435	**58,492**	49,118
Selling, general and administrative expenses	**3,243**	3,144	**9,507**	8,422
Gain on disposal of operating assets		(140)		(136)
Total operating expenses	**24,220**	21,439	**67,999**	57,404
Operating income	**3,113**	2,583	**8,494**	7,274
Interest income	**(3)**	(1)	**(5)**	(3)
Interest expense	**22**	53	**135**	107
Foreign currency exchange gain, net	**(8)**	(6)	**(12)**	(14)
Other (income) expense, net	**(1)**	24	**(1)**	(9)
Income from continuing operations before income tax provision	**3,103**	2,513	**8,377**	7,193
Income tax provision	**1,035**	618	**3,031**	730
Income from continuing operations	**2,068**	1,895	**5,346**	6,463
Income (loss) from discontinued operations, net of tax	**91**	(1,532)	**(216)**	(1,897)
Net income	**$ 2,159**	$ 363	**$ 5,130**	$ 4,566
Income per share from continuing operations				
Basic	**$ 0.39**	$ 0.36	**$ 1.01**	$ 1.23
Diluted	**$ 0.38**	$ 0.36	**$ 1.00**	$ 1.23
Income (loss) per share from discontinued operations, net of tax				
Basic	**$ 0.02**	$ (0.29)	**$ (0.04)**	$ (0.36)

Diluted	**$ 0.02**	$ (0.29)	**$ (0.04)**	$ (0.36)
Net income per share				
Basic	**$ 0.41**	$ 0.07	**$ 0.97**	$ 0.87
Diluted	**$ 0.40**	$ 0.07	**$ 0.96**	$ 0.87
Weighted-average number of common shares (basic)	**5,294**	5,252	**5,290**	5,237
Weighted-average number of common shares (diluted)	**5,345**	5,311	**5,342**	5,274

See notes to unaudited consolidated condensed financial statements.

Table of Contents

SIFCO Industries, Inc. and Subsidiaries
Consolidated Condensed Balance Sheets
(Amounts in thousands, except per share data)

	June 30, 2008 (unaudited)	September 30, 2007
ASSETS		
Current assets:		
Cash and cash equivalents	**$ 7,055**	$ 5,510
Receivables, net	**21,128**	19,473
Inventories	**13,341**	16,897
Refundable income taxes	**20**	
Deferred income taxes	**1,829**	2,423
Prepaid expenses and other current assets	**410**	370
Assets held for sale	**3,532**	3,189
Total current assets	**47,315**	47,862
Property, plant and equipment, net	**11,313**	10,570
Other assets	**3,472**	2,457
Total assets	**$ 62,100**	$ 60,889
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Current maturities of long-term debt	**$ 92**	$ 87
Accounts payable	**9,022**	9,735
Accrued liabilities	**4,835**	5,690
Total current liabilities	**13,949**	15,512
Long-term debt, net of current maturities	**312**	2,986
Deferred income taxes	**3,468**	3,655
Other long-term liabilities	**1,521**	1,958
Shareholders equity:		
Serial preferred shares, no par value, authorized 1,000 shares		
Common shares, par value $1 per share, authorized 10,000 shares; issued and outstanding 5,294 and 5,281 shares at June 30, 2008 and September 30, 2007	**5,294**	5,281
Additional paid-in capital	**6,376**	6,352
Retained earnings	**34,958**	29,828

Accumulated other comprehensive loss	**(3,778)**	(4,683)
Total shareholders equity	**42,850**	36,778
Total liabilities and shareholders equity	**$ 62,100**	$ 60,889

See notes to unaudited consolidated condensed financial statements.

3

Table of Contents

SIFCO Industries, Inc. and Subsidiaries
Consolidated Condensed Statements of Cash Flows
(Unaudited)
(Amounts in thousands)

	Nine Months Ended June 30,	
	2008	**2007**
Cash flows from operating activities:		
Net income	**$ 5,130**	$ 4,566
Loss from discontinued operations, net of tax	**216**	1,897
Adjustments to reconcile net income to net cash provided by (used for) operating activities of continuing operations:		
Depreciation and amortization	**1,102**	1,081
Loss (gain) on disposal of property, plant and equipment	**1**	(136)
Deferred income taxes	**396**	594
Other	**37**	62
Changes in operating assets and liabilities:		
Receivables	**(1,952)**	(4,168)
Inventories	**3,579**	(5,174)
Accounts payable	**40**	(12)
Accrued liabilities	**(902)**	39
Other long-term liabilities	**(1,291)**	12
Other	**(205)**	170
Net cash provided by (used for) operating activities of continuing operations	**6,151**	(1,069)
Net cash used for operating activities of discontinued operations	**(659)**	(3,464)
Cash flows from investing activities**:**		
Capital expenditures	**(1,782)**	(1,051)
Other		96
Net cash used for investing activities of continuing operations	**(1,782)**	(955)
Net cash provided by investing activities of discontinued operations		4,047
Cash flows from financing activities:		
Proceeds from revolving credit agreement	**20,848**	23,104
Repayments of revolving credit agreement	**(23,448)**	(21,373)
Other	**(69)**	434
Net cash provided by (used for) financing activities of continuing operations	**(2,669)**	2,165
Increase in cash and cash equivalents	**1,041**	724
Cash and cash equivalents at the beginning of the period	**5,510**	4,744
Effect of exchange rate changes on cash and cash equivalents	**504**	312

Cash and cash equivalents at the end of the period	**$ 7,055**	$ 5,780
Supplemental disclosure of cash flow information of continuing operations:		
Cash paid for interest	**$ (156)**	$ (81)
Cash paid for income taxes, net	**(2,890)**	(72)

See notes to unaudited consolidated condensed financial statements.

Table of Contents

SIFCO Industries, Inc. and Subsidiaries
Notes to Unaudited Consolidated Condensed Financial Statements
(Dollars in thousands, except share and per share data)

1. Summary of Significant Accounting Policies

A. Principles of Consolidation

The accompanying unaudited consolidated condensed financial statements included herein include the accounts of SIFCO Industries, Inc. and its wholly-owned subsidiaries (the Company). All significant intercompany accounts and transactions have been eliminated. The U.S. dollar is the functional currency for all of the Company s U.S. operations. For these operations, all gains and losses from completed currency transactions are included in income currently. For the Company s non-U.S. subsidiaries, the functional currency is the local currency. Assets and liabilities are translated into U.S. dollars at the rates of exchange at the end of the period, and revenues and expenses are translated using average rates of exchange. Foreign currency translation adjustments are reported as a component of accumulated other comprehensive loss in the consolidated condensed financial statements. In the opinion of management, all adjustments, which include only normal recurring adjustments necessary for a fair presentation of the results of operations, financial position, and cash flows for the periods presented, have been included.

These unaudited consolidated condensed financial statements should be read in conjunction with the consolidated financial statements and related notes included in the Company s fiscal 2007 Annual Report on Form 10-K. The results of operations for any interim period are not necessarily indicative of the results to be expected for other interim periods or the full year. Certain prior period amounts have been reclassified in order to conform to current period classifications.

B. Stock-Based Compensation

The Company has awarded stock options under its shareholder approved 1995 Stock Option Plan (1995 Plan) and 1998 Long-term Incentive Plan (1998 Plan). No further options may be awarded under either the 1995 Plan or the 1998 Plan. Option exercise price is not less than fair market value on date of grant and options are exercisable no later than ten years from date of grant. Options awarded under both Plans generally vest at a rate of 25% per year.

Aggregate option activity is as follows:

	Number of Share Options	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
September 30, 2007	110,500	$ 4.46		
Options exercised	(16,500)	$ 3.69		
June 30, 2008	94,000	$ 4.59	4.5	$ 518
Vested or expected to vest at June 30, 2008	94,000	$ 4.59	4.5	$ 518
Exercisable at June 30, 2008	81,000	$ 4.73	4.1	$ 435

As of June 30, 2008, there was $7 of total unrecognized compensation cost related to the unvested stock options granted under the Plans. The Company expects to recognize this cost over a weighted average period of less than 1.0 year.

In the first quarter of fiscal 2008, the Company adopted the SIFCO Industries, Inc. 2007 Long-Term Incentive Plan (2007 Plan), which plan was approved by the Company s shareholders at its 2008 Annual Meeting on January 29, 2008. The aggregate number of shares that may be awarded under the 2007 Plan is 250,000, subject to an adjustment for the forfeiture of any issued shares. In addition, shares that may be awarded are subject to individual award limitations. The shares awarded under the 2007 Plan may be made in multiple forms including stock options, stock appreciation rights, restricted or unrestricted stock, and performance related shares. Any such awards are exercisable no later than ten years from date of grant.

In late March 2008, the Company began granting performance shares. The performance shares awarded in fiscal 2008 provide for the issuance of the Company s common shares upon the Company achieving certain defined financial performance objectives during a three year award period ending September 30, 2010.

5

The ultimate number of common shares of the Company that may be earned pursuant to an award will range from a minimum of no shares to a maximum of 150% of the initial number of performance shares awarded, depending on the Company s achievement of its financial performance objectives. Compensation expense for the performance shares awarded during fiscal 2008 is being accrued at 50% of the target level and, during each future reporting period, such expense may be subject to adjustment based upon the Company s subsequent estimate of the number of common shares that it expects to issue upon the completion of the performance period. The performance shares were valued at the closing market price of the Company s common shares on the date of grant, and the vesting of such shares is determined at the end of the performance period. Compensation expense related to the performance shares awarded during the second quarter of fiscal 2008 was $19. As of June 30, 2008, there was $172 of total unrecognized compensation cost related to the performance shares awarded under the 2007 Plan. The Company expects to recognize this cost over the next 2.3 years.

The following is a summary of activity related to performance shares:

	Number of Shares	**Weighted Average Fair Value at Date of Grant**
Outstanding at September 30, 2007		
Performance shares awarded	35,000	$ 10.94
Outstanding at June 30, 2008	35,000	$ 10.94

2. Inventories

Inventories consist of:

	June 30, 2008	**September 30, 2007**
Raw materials and supplies	**$ 4,685**	$ 7,579
Work-in-process	**6,142**	6,433
Finished goods	**2,514**	2,885
Total inventories	**$ 13,341**	$ 16,897

Inventories are stated at the lower of cost or market. Cost is determined using the last-in, first-out (LIFO) method for 72% and 80% of the Company s inventories at June 30, 2008 and September 30, 2007, respectively. Cost is determined using the specific identification method for approximately 10% and 7% of the Company s inventories at June 30, 2008 and September 30, 2007, respectively. The first-in, first-out (FIFO) method is used for the remainder of the inventories. If the FIFO method had been used for the inventories for which cost is determined using the LIFO method, inventories would have been $6,994 and $7,191 higher than reported at June 30, 2008 and September 30, 2007, respectively.

3. Comprehensive Income and Accumulated Other Comprehensive Loss

Total comprehensive income is as follows:

	Three Months Ended June 30,	**Nine Months Ended June 30,**

	2008	2007	2008	2007
Net income	**$ 2,159**	$ 363	**$ 5,130**	$ 4,566
Foreign currency translation adjustment	**(42)**	115	**905**	1,848
Minimum pension liability adjustment		958		958
Total comprehensive income	**$ 2,117**	$ 1,436	**$ 6,035**	$ 7,372

Table of Contents

The components of accumulated other comprehensive loss are as follows:

	June 30, 2008	September 30, 2007
Foreign currency translation adjustment	**$ (3,454)**	$ (4,359)
SFAS No. 158 net pension liability adjustment, net of tax	**(324)**	(324)
Total accumulated other comprehensive loss	**$ (3,778)**	$ (4,683)

4. Long-Term Debt

In February 2008, the Company entered into an agreement with its bank to (i) increase the maximum availability under its revolving credit agreement from $6,000 to $8,000, (ii) reduce the interest rate from the bank s base rate plus 0.50% to the bank s base rate, (iii) reduce the commitment fee on the unused balance from 0.38% to 0.35%, (iv) revise its financial covenants and (v) extend the maturity date of its revolving credit agreement from October 1, 2008 to July 1, 2009. The Company was in compliance with all applicable covenants under its revolving credit agreement as of June 30, 2008.

5. Government Grants

The Company received grants from certain government entities as an incentive to invest in facilities, research and employees. The Company has historically elected to treat capital and employment grants as a contingent obligation and does not commence amortizing such grants into income until such time that it is more certain that the Company will not be required to repay a portion of these grants. Capital grants are amortized into income over the estimated useful lives of the related assets. Employment grants are amortized into income over five years.

Certain grants that were subject to repayment expired in the first quarter of fiscal 2007. Therefore, the Company will not be required to repay such grants and, accordingly, the Company recognized grant income of approximately $2,100 in loss from discontinued operations, net of tax, during the nine months ended June 30, 2007 in the accompanying unaudited consolidated condensed statement of operations.

The unamortized portion of deferred grant revenue recorded in other long-term liabilities at June 30, 2008 and September 30, 2007 was $494 and $451, respectively. The majority of the Company s grants are denominated in euros. The Company adjusts its deferred grant revenue balance in response to currency exchange rate fluctuations for as long as such grants are treated as obligations.

6. Income Taxes

For each interim reporting period, the Company makes an estimate of the effective tax rate it expects to be applicable for the full fiscal year. This rate so determined is used in providing for income taxes on a year-to-date basis. The Company s estimated effective tax rate through the third quarter of fiscal 2008 is 36% and differs from the U.S. federal rate due primarily to (i) the impact of state and local income taxes, (ii) a domestic production activities deduction, and (iii) the U.S. recognition of foreign earnings and the valuation of net operating losses from discontinued operations of non-U.S. subsidiaries. The income tax provision consists of the following:

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2008	**2007**	**2008**	**2007**
Current income tax provision:				
U.S. federal	**$ 631**	$ 10	**$ 2,209**	$ 99
U.S. state and local	**86**		**225**	
Non-U.S	**87**	14	**201**	37
Total current tax provision	**804**	24	**2,635**	136

Deferred income tax provision (benefit):				
U.S. federal	**202**	594	**345**	594
U.S. state and local	**29**		**105**	
Non-U.S			**(54)**	
Total deferred tax provision	**231**	594	**396**	594
Income tax provision	**$ 1,035**	$ 618	**$ 3,031**	$ 730

7

Effective October 1, 2007, the Company adopted Financial Accounting Standards Board (FASB) Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes an interpretation of Statement of Financial Accounting Standards No. 109 (SFAS No. 109), Accounting for Income Taxes . Previously, the Company had accounted for tax contingencies in accordance with SFAS No. 5, Accounting for Contingencies. As required by FIN 48, which clarifies SFAS No. 109, Accounting for Income Taxes, the Company recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority would, more likely than not, sustain the position following an audit. For tax positions meeting that threshold, the amount recognized in the financial statements is the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement with the relevant tax authority. At the adoption date, the Company applied FIN 48 to all positions for which the statute of limitations remained open. The adoption of FIN 48 did not have a material impact on the Company s financial position, cash flows and results of operations. The Company has no material unrecognized tax benefits at June 30, 2008 and October 1, 2007.

The Company is subject to U.S. federal income tax and income taxes in various states and foreign jurisdictions. Tax regulations within each jurisdiction are subject to the interpretation of the related tax laws and regulations and require significant judgment to apply. With few exceptions, the Company is no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for fiscal years that ended prior to September 30, 2001.

It is the Company s continuing policy to recognize any interest related to uncertain tax positions in interest expense and any penalties related to uncertain tax positions in selling, general and administrative expense. The Company has not recorded any significant interest or penalties related to uncertain tax positions as of June 30, 2008.

7. Retirement Benefit Plans

The Company and certain of its subsidiaries sponsor defined benefit pension plans covering most of its employees. The components of net periodic benefit cost (income) of the Company s defined benefit plans are as follows:

	Three Months Ended June 30,		**Nine Months Ended June 30,**	
	2008	**2007**	**2008**	**2007**
Service cost	**$ 61**	$ 70	**$ 182**	$ 210
Interest cost	**237**	252	**712**	756
Expected return on plan assets	**(358)**	(301)	**(1,073)**	(902)
Amortization of prior service cost	**33**	33	**99**	99
Amortization of net loss (gain)	**(18)**	32	**(54)**	95