Dorman Products, Inc.
Form 10-Q
August 01, 2018
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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 June 30, 2018

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: 0-18914

Dorman Products, Inc.

(Exact name of registrant as specified in its charter)

Pennsylvania	23-2078856
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

3400 East Walnut Street, Colmar, Pennsylvania	18915
(Address of principal executive offices)	(Zip Code)

(215) 997-1800

(Registrant's telephone number, including area code)

N/A

(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 No

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 No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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 July 30, 2018, the registrant had 33,185,857 shares of common stock, par value $0.01 per share, outstanding.

DORMAN PRODUCTS, INC. AND SUBSIDIARIES

INDEX TO QUARTERLY REPORT ON FORM 10-Q

June 30, 2018

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

DORMAN PRODUCTS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(UNAUDITED)

	Thirteen Weeks Ended	
(in thousands, except per share data)	June 30, 2018	July 1, 2017
Net sales	$238,147	$229,262
Cost of goods sold	145,446	138,410
Gross profit	92,701	90,852
Selling, general and administrative expenses	49,921	45,853
Income from operations	42,780	44,999
Other income, net	73	241
Income before income taxes	42,853	45,240
Provision for income taxes	8,514	16,803
Net income	$34,339	$28,437
Earnings Per Share:		
Basic	$1.04	$0.83
Diluted	$1.03	$0.83
Weighted Average Shares Outstanding:		
Basic	33,146	34,128
Diluted	33,226	34,225

See accompanying Notes to Consolidated Financial Statements

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DORMAN PRODUCTS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(UNAUDITED)

	Twenty-Six Weeks Ended	
(in thousands, except per share data)	June 30, 2018	July 1, 2017
Net sales	$465,409	$450,887
Cost of goods sold	284,072	271,292
Gross profit	181,337	179,595
Selling, general and administrative expenses	98,563	89,554
Income from operations	82,774	90,041
Other income, net	224	305
Income before income taxes	82,998	90,346
Provision for income taxes	18,013	32,722
Net income	$64,985	$57,624
Earnings Per Share:		
Basic	$1.95	$1.68
Diluted	$1.95	$1.68
Weighted Average Shares Outstanding:		
Basic	33,273	34,256
Diluted	33,355	34,350

See accompanying Notes to Consolidated Financial Statements

DORMAN PRODUCTS, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

(in thousands, except for share data)	June 30, 2018	December 30, 2017
Assets		
Current assets:		
Cash and cash equivalents	$74,810	$ 71,691
Accounts receivable, less allowance for doubtful accounts and customer credits of $89,883 and $97,193	282,681	241,880
Inventories	218,523	212,149
Prepaids and other current assets	8,589	7,129
Total current assets	584,603	532,849
Property, plant and equipment, net	93,325	92,692
Goodwill	66,918	65,999
Intangible assets, net	21,230	22,158
Deferred tax asset, net	5,406	7,884
Other assets	44,366	44,342
Total	$815,848	$ 765,924
Liabilities and shareholders’ equity		
Current liabilities:		
Accounts payable	$97,981	$ 80,218
Accrued compensation	7,503	12,162
Other accrued liabilities	17,077	18,401
Total current liabilities	122,561	110,781
Other long-term liabilities	13,706	13,732
Deferred tax liabilities, net	5,565	6,604
Commitments and contingencies		
Shareholders’ Equity:		
Common stock, par value $0.01; authorized 50,000,000 shares; issued and outstanding 33,225,771 and 33,571,524 in 2018 and 2017, respectively	332	336
Additional paid-in capital	46,365	44,812
Retained earnings	627,319	589,659
Total shareholders’ equity	674,016	634,807
Total	$815,848	$ 765,924

See accompanying Notes to Consolidated Financial Statements

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DORMAN PRODUCTS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

	Twenty-Six Weeks Ended	
(in thousands)	June 30, 2018	July 1, 2017
Cash Flows from Operating Activities:		
Net income	$64,985	$57,624
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation, amortization and accretion	13,004	10,192
Provision for doubtful accounts	(661)	150
Provision (benefit) for deferred income taxes	2,474	(2,666)
Provision for non-cash stock compensation	1,998	1,478
Changes in assets and liabilities:		
Accounts receivable	(40,180)	(38)
Inventories	(6,122)	(29,690)
Prepaids and other current assets	(2,018)	(1,932)
Other assets	565	(2,503)
Accounts payable	17,816	18,158
Accrued compensation and other liabilities	(6,256)	(8,850)
Cash provided by operating activities	45,605	41,923
Cash Flows from Investing Activities:		
Acquisition, net of cash acquired	(564)	(3,127)
Property, plant and equipment additions	(11,416)	(11,932)
Purchase of investments	-	(10,000)
Cash used in investing activities	(11,980)	(25,059)
Cash Flows from Financing Activities:		
Contingent consideration	(2,037)	-
Other stock related activity	(318)	(1,043)
Purchase and cancellation of common stock	(28,066)	(35,734)
Cash used in financing activities	(30,421)	(36,777)
Effect of exchange rate changes on Cash and Cash Equivalents	(85)	-
Net Increase in Cash and Cash Equivalents	3,119	(19,913)
Cash and Cash Equivalents, Beginning of Period	71,691	149,121
Cash and Cash Equivalents, End of Period	$74,810	$129,208
Supplemental Cash Flow Information		
Cash paid for interest expense	$133	$129
Cash paid for income taxes	$13,420	$38,679

See accompanying Notes to Consolidated Financial Statements

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DORMAN PRODUCTS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE TWENTY-SIX WEEKS ENDED JUNE 30, 2018 AND JULY 1, 2017

(UNAUDITED)

1. Basis of Presentation

As used herein, unless the context otherwise requires, “Dorman”, the “Company”, “we”, “us”, or “our” refers to Dorman Products, Inc. and its subsidiaries. Our ticker symbol on the NASDAQ Global Select Market is “DORM”.

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the U.S. for interim financial information and in accordance with the rules and regulations of the U.S. Securities and Exchange Commission (“SEC”). However, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of only normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the twenty-six weeks ended June 30, 2018 are not necessarily indicative of the results that may be expected for the fiscal year ending December 29, 2018. We may experience significant fluctuations from quarter to quarter in our results of operations due to the timing of orders placed by our customers. The introduction of new products and product lines to customers may cause significant fluctuations from quarter to quarter. These financial statements should be read in conjunction with the consolidated financial statements and footnotes thereto included in our Annual Report on Form 10-K for the fiscal year ended December 30, 2017.

2. Business Acquisitions and Investments

On October 26, 2017, we acquired 100% of the outstanding stock of MAS Automotive Distribution Inc. (“MAS Industries” or “MAS”), a privately-held manufacturer of premium chassis and control arms based in Montreal, Canada. The purchase price was $67.2 million net of $3.3 million of cash acquired and including contingent consideration at fair value and other purchase price adjustments.

We believe MAS is complementary to our business and growth strategy. We see opportunities to leverage MAS’ existing presence in the automotive aftermarket, as well as our product development capabilities and financial resources to accelerate the growth of MAS’ premium chassis and control arm products.

We have included the results of MAS in our Consolidated Financial Statements since the acquisition date of October 26, 2017. The Consolidated Statement of Operations for the twenty-six weeks ended June 30, 2018 includes $20.2 million of net sales and an immaterial amount of net income related to MAS. The Consolidated Balance Sheets as of June 30, 2018 and December 30, 2017 reflects the acquisition of MAS Industries, effective October 26, 2017.

The following table summarizes the preliminary fair value of the total consideration at October 26, 2017:

(in thousands)	Total Acquisition Date Fair Value
Cash consideration (net of $3.3 million cash acquired)	$ 56,859

Contingent cash consideration	7,982
Seller liability assumed	896
Working capital adjustment	1,486
Total consideration assigned to net assets acquired	$ 67,223

Included in the table above is $8.0 million of estimated contingent payments which represents the fair value of the estimated payments which will become due if certain sales thresholds are achieved through December 2020. The fair value of the contingent cash consideration was estimated by using an option pricing model framework, which represents our own assumptions and data, and is based on our best available information. As of June 30, 2018, we had $8.0 million recorded which includes $0.2 million of accretion which was included in Selling, General and Administrative expenses for the twenty-six weeks ended June 30, 2018, related to this payment. The maximum contingent payment would be $11.7 million. Additionally, during the thirteen weeks ended June 30, 2018, we finalized working capital and other purchase price adjustments based on the MAS standalone audited 2017 financial statements, resulting in a payment to the former shareholder of $1.5 million. This amount had previously been accrued on our Consolidated Balance Sheet.

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The transaction was accounted for as a business combination under the acquisition method of accounting. Accordingly, the assets acquired and liabilities assumed were recorded at fair value, with the remaining purchase price recorded as goodwill. The following table summarizes the preliminary fair values of the assets acquired and liabilities assumed as of October 26, 2017 (in thousands):

	October 26, 2017 (As initially reported)	Measurement period adjustments	October 26, 2017 (As adjusted)
Current assets (net of $3.3 million cash acquired)	$ 21,756	$ 90	$ 21,846
Property, plant and equipment	1,615	-	1,615
Intangible assets	20,440	-	20,440
Goodwill	35,624	(193)	35,431
Total assets acquired	79,435	(103)	79,332
Current liabilities	5,691	(50)	5,641
Long-term liabilities	6,468	-	6,468
Total liabilities assumed	12,159	(50)	12,109
Net assets acquired	$ 67,276	$ (53)	$ 67,223

The estimated fair value of the MAS assets acquired and liabilities assumed are provisional as of June 30, 2018 and are based on information that is currently available. Additional information about conditions that existed as of the date of acquisition are being gathered to finalize these provisional measurements, particularly with respect to inventory valuation. Accordingly, the measurement of the MAS assets acquired and liabilities assumed may change significantly upon completion of the purchase price allocation, both of which are expected to occur no later than one year from the acquisition date.

The valuation of the intangible assets acquired and related amortization periods are as follows:

(in thousands)	Valuation	Amortization Period (in years)
Customer relationships	$ 14,840	8-12
Tradenames	5,600	15
Total	$ 20,440	

The fair values of the Customer Relationships and Tradenames were estimated using a discounted present value income approach. Under this method, an intangible asset’s fair value is equal to the present value of the incremental after-tax cash flows (excess earnings) attributable solely to the intangible asset over its remaining useful life. To calculate fair value, we used cash flows discounted at rates ranging from 15% to 17%, which were considered appropriate given the inherent risk associated with each type of asset. We believe that the level and timing of cash flows appropriately reflect market participant assumptions.

The goodwill recognized is attributable primarily to strategic and synergistic opportunities related to existing automotive aftermarket businesses, the assembled workforce of MAS and other factors. The goodwill is expected to be deductible for tax purposes.

Pro Forma Financial Information (Unaudited)

The unaudited pro forma information for the periods set forth below give effect to the MAS acquisition as if it occurred as of December 27, 2015, the start of our 2016 fiscal year. The pro forma information is presented for informational purposes only and is not necessarily indicative of the results of the operations that actually would have been achieved had the acquisition been consummated as of that time:

(in thousands)	Twenty-Six Weeks Ended July 1, 2017
Net sales	$ 469,045
Net income	$ 57,850
Diluted earnings per share	$ 1.68

The unaudited pro forma net income for the twenty-six week period ending July 1, 2017 was adjusted to include amortization of intangible assets, accretion for contingent consideration liabilities and to exclude financing costs of MAS which we do not believe would have occurred.

3. Sales of Accounts Receivable

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We have entered into several customer sponsored programs administered by unrelated financial institutions that permit us to sell certain accounts receivable at discounted rates to the financial institutions. Transactions under these agreements were accounted for as sales of accounts receivable and were removed from our Consolidated Balance Sheet at the time of the sales transactions. Pursuant to these agreements, we sold $282.1 million and $299.1 million of accounts receivable during the twenty-six weeks ended June 30, 2018 and July 1, 2017, respectively. If receivables had not been sold, $358.3 million and $380.8 million of additional accounts receivable would have been outstanding at June 30, 2018 and December 30, 2017, respectively, based on standard payment terms. Selling, general and administrative expenses for the twenty-six weeks ended June 30, 2018 and July 1, 2017 included $6.7 million and $5.6 million, respectively, in financing costs associated with these accounts receivable sales programs.

4. Inventories

Inventories include the cost of material, freight, direct labor and overhead utilized in the processing of our products, and are stated at the lower of cost or net realizable value. Inventories were as follows:

	June 30,	December 30,
(in thousands)	2018	2017
Bulk product	$93,751	$ 82,010
Finished product	121,363	126,827
Packaging materials	3,409	3,312
Total	$218,523	$ 212,149

5. Goodwill and Intangible Assets

Goodwill

Goodwill included the following:

	June 30,	December 30,
(in thousands)	2018	2017
Balance at beginning of period	$65,999	$ 28,146
Goodwill acquired	1,112	37,853
Measurement period adjustments	(193)	-
Balance at end of period	$66,918	$ 65,999

Intangible Assets

Intangible assets included the following:

(in thousands)	June 30, 2018	December 30, 2017

	Weighted Average Amortization Period	Gross Carrying Value	Accumulated Amortization	Net Carrying Value	Gross Carrying Value	Accumulated Amortization	Net Carrying Value
Intangible assets subject to amortization							
Tradenames	14.3	$5,600	$ 213	$5,387	$5,600	$ 62	$5,538
Customer relationships	9.6	17,049	1,536	15,513	17,049	772	16,277
Technology	13.5	367	37	330	367	24	343
Total		$23,016	$ 1,786	$21,230	$23,016	$ 858	$22,158

Amortization expense was $1.1 million and less than $0.1 million for the twenty-six weeks ended June 30, 2018 and July 1, 2017, respectively.

6. Revenue Recognition

The FASB issued an accounting standard update in May 2014 regarding the accounting for and disclosure of revenue. Specifically, the update outlined a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers, which will be common to both U.S. GAAP and International Financial Reporting Standards.

Our primary source of revenue is from contracts with and purchase orders from customers. Revenue is recognized from product sales when goods are shipped, title and risk of loss and control have been transferred to the customer, and collection is reasonably assured. We estimate the transaction price at the inception of a contract or upon fulfilling a purchase order, including any variable consideration, and will update the estimate for changes in circumstances. We utilize the most likely amount method consistently to estimate the effect of uncertainty on the amount of variable consideration to which we would be entitled. The most likely amount method considers the single most likely amount from a range of possible consideration amounts. This method is utilized for all of our variable consideration.

We record estimates for cash discounts, product returns, promotional rebates, core return deposits and other discounts in the period the related product revenue is recognized ("Customer Credits"). The provision for Customer Credits is recorded as a reduction from gross sales and reserves for Customer Credits are shown as a reduction of accounts receivable. Accrued customer rebates which we expect to settle in cash are classified as other accrued liabilities. Actual Customer Credits have not differed materially from estimated amounts for each period presented. Amounts billed to customers for shipping and handling are included in net sales. Costs associated with shipping and handling are included in cost of goods sold. We have concluded that our estimates of variable consideration are not constrained according to the definition of the new standard.

All of our revenue was recognized under the point of time approach in accordance with the revenue standard during the twenty-six weeks ended June 30, 2018 and July 1, 2017, respectively. Also, we do not have significant financing arrangements with our customers, as our credit terms are all less than one year. Lastly, we do not receive noncash consideration (such as materials or equipment) from our customers to facilitate the fulfillment of our contracts.

Five-step model

We apply the FASB's guidance on revenue recognition, which requires us to recognize the amount of revenue and consideration which we expect to receive in exchange for goods or services transferred to our customers. To do this, we apply the five-step model prescribed by the FASB, which requires us to: (i) identify the contract with a customer; (ii) identify the performance obligations in the contract; (iii) determine the transaction price; (iv) allocate the transaction price to the performance obligations in the contract; and (v) recognize revenue when, or as, we satisfy a performance obligation.

Contract Assets and Liabilities

We recognize a receivable or contract asset when we perform a service or transfer a good in advance of receiving consideration.

- A receivable is recorded when our right to consideration is unconditional and only the passage of time is required before payment of that consideration is due.

- A contract asset is recorded when our right to consideration in exchange for good or services that we have transferred to a customer is conditional on something other than the passage of time. We did not have any contract assets recorded as of June 30, 2018 or December 30, 2017.

We recognize a contract liability when we receive consideration, or if we have the unconditional right to receive consideration, in advance of satisfying the performance obligation. A contract liability is our obligation to transfer goods or services to a customer for which we have received consideration, or an amount of consideration is due from the customer. We did not have any contract liabilities recorded as of June 30, 2018 or December 30, 2017.

Disaggregated Revenue

The following tables present our disaggregated net sales by Type of Major Good / Product Line, and Geography.

	Thirteen Weeks Ended		Twenty-Six Weeks Ended	
(in thousands)	June 30, 2018	July 1, 2017	June 30, 2018	July 1, 2017
Powertrain	$99,224	$		