

AUTOZONE INC
Form 10-Q
March 22, 2016
Table of Contents

UNITED STATES
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 February 13, 2016, 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 1-10714

AUTOZONE, INC.
(Exact name of registrant as specified in its charter)

Nevada (State or other jurisdiction of	62-1482048 (I.R.S. Employer
incorporation or organization)	Identification No.)
123 South Front Street, Memphis, Tennessee (Address of principal executive offices)	38103 (Zip Code)
(901) 495-6500 (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 periods 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, 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 <input checked="" type="checkbox"/>	Accelerated filer <input type="checkbox"/>
Non-accelerated filer <input type="checkbox"/>	Smaller reporting company <input type="checkbox"/>

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock, \$.01 Par Value 29,858,892 shares outstanding as of March 18, 2016.

Table of Contents

TABLE OF CONTENTS

PART I.	<u>FINANCIAL INFORMATION</u>	3
Item 1.	<u>Financial Statements</u>	3
	<u>CONDENSED CONSOLIDATED BALANCE SHEETS</u>	3
	<u>CONDENSED CONSOLIDATED STATEMENTS OF INCOME</u>	4
	<u>CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME</u>	5
	<u>CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS</u>	6
	<u>NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS</u>	7
	<u>REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM</u>	16
Item 2.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	17
Item 3.	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	24
Item 4.	<u>Controls and Procedures</u>	24
Item 4T.	<u>Controls and Procedures</u>	24
PART II.	<u>OTHER INFORMATION</u>	25
Item 1.	<u>Legal Proceedings</u>	25
Item 1A.	<u>Risk Factors</u>	25
Item 2.	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	25
Item 3.	<u>Defaults Upon Senior Securities</u>	25
Item 4.	<u>Mine Safety Disclosures</u>	26
Item 5.	<u>Other Information</u>	26
Item 6.	<u>Exhibits</u>	26
	<u>SIGNATURES</u>	27
	<u>EXHIBIT INDEX</u>	28

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements.****AUTOZONE, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS**

(Unaudited)

<i>(in thousands)</i>	February 13, 2016	August 29, 2015
Assets		
Current assets:		
Cash and cash equivalents	\$ 207,958	\$ 175,309
Accounts receivable	295,792	247,872
Merchandise inventories	3,590,687	3,421,635
Other current assets	115,376	121,847
Deferred income taxes		3,631
Total current assets	4,209,813	3,970,294
Property and equipment:		
Property and equipment	6,021,684	5,891,707
Less: Accumulated depreciation and amortization	(2,476,802)	(2,386,075)
	3,544,882	3,505,632
Goodwill	391,887	391,887
Deferred income taxes	23,575	42,615
Other long-term assets	196,257	191,921
	611,719	626,423
	\$ 8,366,414	\$ 8,102,349
Liabilities and Stockholders Deficit		
Current liabilities:		
Accounts payable	\$ 3,912,107	\$ 3,864,168
Accrued expenses and other	535,237	531,561
Income taxes payable	89,913	58,082
Deferred income taxes		259,062
Short-term borrowings	457,404	
Total current liabilities	4,994,661	4,712,873

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Long-term debt	4,387,811	4,624,876
Deferred income taxes	248,653	
Other long-term liabilities	476,602	465,990
Commitments and contingencies		
Stockholders' deficit:		
Preferred stock, authorized 1,000 shares; no shares issued		
Common stock, par value \$.01 per share, authorized 200,000 shares; 30,142 shares issued and 30,101 shares outstanding as of February 13, 2016; 32,098 shares issued and 30,659 shares outstanding as of August 29, 2015	301	321
Additional paid-in capital	953,071	938,355
Retained deficit	(2,356,468)	(1,418,738)
Accumulated other comprehensive loss	(307,849)	(249,518)
Treasury stock, at cost	(30,368)	(971,810)
Total stockholders' deficit	(1,741,313)	(1,701,390)
	\$ 8,366,414	\$ 8,102,349

See Notes to Condensed Consolidated Financial Statements.

Table of Contents**AUTOZONE, INC.****CONDENSED CONSOLIDATED STATEMENTS OF INCOME**

(Unaudited)

<i>(in thousands, except per share data)</i>	Twelve Weeks Ended		Twenty-Four Weeks Ended	
	February 13, 2016	February 14, 2015	February 13, 2016	February 14, 2015
Net sales	\$ 2,257,192	\$ 2,143,651	\$ 4,643,235	\$ 4,403,916
Cost of sales, including warehouse and delivery expenses	1,066,596	1,023,618	2,199,705	2,107,222
Gross profit	1,190,596	1,120,033	2,443,530	2,296,694
Operating, selling, general and administrative expenses	807,936	758,764	1,622,875	1,526,863
Operating profit	382,660	361,269	820,655	769,831
Interest expense, net	32,832	34,536	67,842	71,596
Income before income taxes	349,828	326,733	752,813	698,235
Income taxes	121,215	115,010	266,088	248,202
Net income	\$ 228,613	\$ 211,723	\$ 486,725	\$ 450,033
Weighted average shares for basic earnings per share	30,170	31,903	30,334	32,018
Effect of dilutive stock equivalents	608	637	624	633
Weighted average shares for diluted earnings per share	30,778	32,540	30,958	32,651
Basic earnings per share	\$ 7.58	\$ 6.64	\$ 16.05	\$ 14.06
Diluted earnings per share	\$ 7.43	\$ 6.51	\$ 15.72	\$ 13.78

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

AUTOZONE, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

<i>(in thousands)</i>	Twelve Weeks Ended		Twenty-Four Weeks Ended	
	February 13, 2016	February 14, 2015	February 13, 2016	February 14, 2015
Net income	\$ 228,613	\$ 211,723	\$ 486,725	\$ 450,033
Other comprehensive loss:				
Pension liability adjustments, net of taxes ⁽¹⁾	1,479	1,268	2,713	2,485
Foreign currency translation adjustments	(67,723)	(40,492)	(59,936)	(58,853)
Unrealized gains (losses) on marketable securities, net of taxes ⁽²⁾	148	(50)	86	(88)
Net derivative activities, net of taxes ⁽³⁾	(1,358)	(161)	(1,194)	(227)
Total other comprehensive loss	(67,454)	(39,435)	(58,331)	(56,683)
Comprehensive income	\$ 161,159	\$ 172,288	\$ 428,394	\$ 393,350

(1) Pension liability adjustments are presented net of taxes of \$945 in fiscal 2016 and \$795 in fiscal 2015 for the twelve weeks ended and \$2,135 in fiscal 2016 and \$1,642 in fiscal 2015 for the twenty-four weeks ended.

(2) Unrealized gains (losses) on marketable securities are presented net of taxes of \$79 in fiscal 2016 and \$26 in fiscal 2015 for the twelve weeks ended and \$46 in fiscal 2016 and \$47 in fiscal 2015 for the twenty-four weeks ended.

(3) Net derivative activities are presented net of taxes of \$1,124 in fiscal 2016 and \$179 in fiscal 2015 for the twelve weeks ended and \$1,209 in fiscal 2016 and \$215 in fiscal 2015 for the twenty-four weeks ended.

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

AUTOZONE, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

<i>(in thousands)</i>	Twenty-Four Weeks Ended	
	February 13, 2016	February 14, 2015
Cash flows from operating activities:		
Net income	\$ 486,725	\$ 450,033
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of property and equipment and intangibles	134,936	120,912
Amortization of debt origination fees	3,538	2,918
Income tax benefit from exercise of stock options	(31,864)	(28,619)
Deferred income taxes	10,093	(9,031)
Share-based compensation expense	18,547	20,200
Changes in operating assets and liabilities:		
Accounts receivable	(50,087)	21,377
Merchandise inventories	(193,376)	(277,854)
Accounts payable and accrued expenses	72,158	103,922
Income taxes payable	65,222	79,774
Other, net	14,661	(7,094)
Net cash provided by operating activities	530,553	476,538
Cash flows from investing activities:		
Capital expenditures	(186,591)	(186,174)
Acquisition of business, net of cash		(75,744)
Purchase of intangibles	(10,000)	(10,000)
Purchase of marketable securities	(67,201)	(21,679)
Proceeds from sale of marketable securities	61,982	19,595
Disposal of capital assets and other, net	1,164	2,550
Net cash used in investing activities	(200,646)	(271,452)
Cash flows from financing activities:		
Net proceeds from commercial paper	518,500	604,500
Repayment of debt	(300,000)	(500,000)
Net proceeds from sale of common stock	31,425	38,110
Purchase of treasury stock	(550,057)	(325,667)
Income tax benefit from exercise of stock options	31,864	28,619
Payments of capital lease obligations	(19,769)	(18,169)
Other, net	(217)	(2,087)

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Net cash used in financing activities	(288,254)	(174,694)
Effect of exchange rate changes on cash	(9,004)	(3,338)
Net increase in cash and cash equivalents	32,649	27,054
Cash and cash equivalents at beginning of period	175,309	124,485
Cash and cash equivalents at end of period	\$ 207,958	\$ 151,539

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

AUTOZONE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note A General

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with instructions to Form 10-Q and Article 10 of Regulation S-X of the Securities and Exchange Commission's (the "SEC") rules and regulations. Accordingly, 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, including normal recurring accruals, considered necessary for a fair presentation have been included. For further information, refer to the consolidated financial statements and related notes included in the AutoZone, Inc. ("AutoZone" or the "Company") Annual Report on Form 10-K for the year ended August 29, 2015.

Operating results for the twelve and twenty-four weeks ended February 13, 2016 are not necessarily indicative of the results that may be expected for the fiscal year ending August 27, 2016. Each of the first three quarters of AutoZone's fiscal year consists of 12 weeks, and the fourth quarter consists of 16 or 17 weeks. The fourth quarters for fiscal 2016 and 2015 each have 16 weeks. Additionally, the Company's business is somewhat seasonal in nature, with the highest sales generally occurring during the months of February through September and the lowest sales generally occurring in the months of December and January.

Recently Adopted Accounting Pronouncements: In November 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2015-17, *Income Taxes - Balance Sheet Classification of Deferred Taxes (Topic 740)*. ASU 2015-17 requires all deferred tax liabilities and assets to be presented in the balance sheet as noncurrent. The Company early adopted this standard prospectively during the quarter ended February 13, 2016. The adoption of this standard resulted in the reclassification of \$3.5 million from current Deferred income tax assets in the Consolidated Balance Sheet as of February 13, 2016 to noncurrent Deferred income tax assets and \$251.2 million from current Deferred income tax liabilities to noncurrent Deferred income tax liabilities. No prior periods were retrospectively adjusted.

Recently Issued Accounting Pronouncements: In September 2015, the FASB issued ASU 2015-16, *Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments*. ASU 2015-16 requires an acquirer to recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined, including the cumulative effect of the change in provisional amount, as if the accounting had been completed at the acquisition date. The Company does not expect the provision of ASU 2015-16 to have a material impact on its consolidated financial statements. This update will be effective for the Company beginning with its fiscal 2017 first quarter.

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. ASU 2016-01 requires that all financial assets and liabilities not accounted for under the equity method to be measured at fair value with the changes in fair value recognized in net income. The amendments in this update also require an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. In addition, the amendments in this update supersede the requirement to

disclose the methods and significant assumptions used in calculating the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet for public business entities. The Company can early adopt the provision requiring it to recognize in other comprehensive income the fair value change from instrument-specific credit risk measured using the fair value option for financial instruments. Except for this early application guidance, early adoption is not permitted. The Company is still evaluating the effects that the provision of ASU 2016-01 will have on its consolidated financial statements. This update will be effective for the Company beginning with its fiscal 2019 first quarter.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*. ASU 2016-02 requires an entity to recognize a right-of-use asset and lease liability for all leases with terms of more than 12 months. Recognition, measurement and presentation of expenses will depend on classification as a finance or operating lease. The amendments also require certain quantitative and qualitative disclosures about leasing arrangements. Early adoption is permitted. The updated guidance requires a modified retrospective adoption. The Company is still evaluating the effects that the provision of ASU 2016-02 will have on its consolidated financial statements. This update will be effective for the Company beginning with its fiscal 2020 first quarter.

Note B Share-Based Payments

AutoZone recognizes compensation expense for share-based payments based on the fair value of the awards at the grant date. Share-based payments include stock option grants, restricted stock grants, restricted stock unit grants and the discount on shares sold to employees under share purchase plans. Additionally, directors' fees are paid in restricted stock units with value equivalent to the value of shares of common stock as of the grant date. The change in fair value of liability-based stock awards is also recognized in share-based compensation expense.

Total share-based compensation expense (a component of Operating, selling, general and administrative expenses) was \$9.9 million for the twelve week period ended February 13, 2016, and was \$11.4 million for the comparable prior year period. Share-based compensation expense was \$18.5 million for the twenty-four week period ended February 13, 2016, and was \$20.2 million for the comparable prior year period.

Table of Contents

During the twenty-four week period ended February 13, 2016, 149,832 stock options were exercised at a weighted average exercise price of \$213.20. In the comparable prior year period, 210,976 stock options were exercised at a weighted average exercise price of \$183.26.

The Company made stock option grants of 375,815 shares during the twenty-four week period ended February 13, 2016, and granted options to purchase 328,060 shares during the comparable prior year period. The weighted average fair value of the stock option awards granted during the twenty-four week periods ended February 13, 2016, and February 14, 2015, using the Black-Scholes-Merton multiple-option pricing valuation model, was \$156.19 and \$106.17 per share, respectively, using the following weighted average key assumptions:

	Twenty-Four Weeks Ended	
	February 13, 2016	February 14, 2015
Expected price volatility	18%	20%
Risk-free interest rate	1.5%	1.4%
Weighted average expected lives (in years)	5.7	5.1
Forfeiture rate	10%	9%
Dividend yield	0%	0%

See AutoZone's Annual Report on Form 10-K for the year ended August 29, 2015, for a discussion regarding the methodology used in developing AutoZone's assumptions to determine the fair value of the option awards and a description of AutoZone's 2011 Equity Incentive Award Plan, the 2011 Director Compensation Program and the 2014 Director Compensation Plan.

For the twelve week period ended February 13, 2016, 24,570 stock options were excluded from the diluted earnings per share computation because they would have been anti-dilutive. For the comparable prior year period, 600 anti-dilutive shares were excluded from the dilutive earnings per share computation. There were 24,570 anti-dilutive shares excluded from the diluted earnings per share computation for the twenty-four week period ended February 13, 2016, and 600 anti-dilutive shares excluded for the comparable prior year period.

During the second quarter of fiscal 2016, the Company's stockholders approved the Amended and Restated AutoZone, Inc. 2011 Equity Incentive Award Plan (the Amended 2011 Equity Plan). The Amended 2011 Equity Plan imposes a maximum limit on the compensation, measured as the sum of any cash compensation and the aggregate grant date fair value of awards granted under the Amended 2011 Equity Plan, which may be paid to non-employee directors for such service during any calendar year. The Amended 2011 Equity Plan also applies a ten-year term on the Amended 2011 Equity Plan through December 16, 2025 and extends the Company's ability to grant incentive stock options through October 7, 2025.

Note C Fair Value Measurements

The Company defines fair value as the price received to transfer an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Company uses a hierarchy of valuation inputs to measure fair value.

The hierarchy prioritizes the inputs into three broad levels:

Level 1 inputs unadjusted quoted prices in active markets for identical assets or liabilities that the Company has the ability to access. An active market for the asset or liability is one in which transactions for the asset or liability occur with sufficient frequency and volume to provide ongoing pricing information.

Level 2 inputs inputs other than quoted market prices included in Level 1 that are observable, either directly or indirectly, for the asset or liabi