FLOW INTERNATIONAL CORP
Form 10-Q
December 03, 2010

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 October 31, 2010

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 001-34443

FLOW INTERNATIONAL CORPORATION

WASHINGTON	**91-1104842**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

23500 64th Avenue South
Kent, Washington 98032
(253) 850-3500

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 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 o 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 þ	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 þ

The registrant had 47,169,032 shares of Common Stock, $0.01 par value per share, outstanding as of November 24, 2010.

FLOW INTERNATIONAL CORPORATION
INDEX

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

FLOW INTERNATIONAL CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except par values)

(unaudited)

	October 31, 2010	April 30, 2010
ASSETS		
Current Assets:		
Cash and Cash Equivalents	$ 6,892	$ 6,367
Restricted Cash	695	639
Receivables, net	40,437	35,749
Inventories, net	27,213	22,503
Deferred Income Taxes, net	2,521	2,486
Other Current Assets	5,920	6,351
Total Current Assets	83,678	74,095
Property and Equipment, net	19,862	21,769
Intangible Assets, net	4,708	4,504
Deferred Income Taxes, net	25,689	26,330
Other Long-Term Assets	4,327	4,511
Total Assets	**$ 138,264**	**$ 131,209**
LIABILITIES AND SHAREHOLDERS EQUITY		
Current Liabilities:		
Notes Payable	$ 2,050	$ 350
Current Portion of Long-Term Obligations	28	61
Accounts Payable	15,354	15,306
Accrued Payroll and Related Liabilities	6,887	5,938
Taxes Payable and Other Accrued Taxes	2,273	1,329
Deferred Income Taxes	1,141	1,086
Deferred Revenue and Customer Deposits	12,120	10,146
Other Accrued Liabilities	8,027	7,966
Total Current Liabilities	47,880	42,182
Deferred Income Taxes	3,955	3,856
Subordinated Notes	8,327	7,954
Other Long-Term Liabilities	1,823	1,593
Total Liabilities	**61,985**	**55,585**
Commitments and Contingencies		
Shareholders Equity:		

Series A 8% Convertible Preferred Stock, $.01 par value, 1,000 shares authorized; no shares issued and outstanding		
Common Stock, $.01 par value, 84,000 shares authorized; 47,168 and 46,927 shares issued and outstanding	467	465
Capital in Excess of Par	160,466	159,605
Accumulated Deficit	(80,750)	(79,887)
Accumulated Other Comprehensive Income (Loss):		
Defined Benefit Plan Obligation, net of income tax	9	9
Cumulative Translation Adjustment, net of income tax	(3,913)	(4,568)
Total Shareholders Equity	**76,279**	**75,624**
Total Liabilities and Shareholders Equity	**$ 138,264**	**$ 131,209**

See Accompanying Notes to Condensed Consolidated Financial Statements

1

Table of Contents

FLOW INTERNATIONAL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share amounts)
(unaudited)

	Three Months Ended October 31,		Six Months Ended October 31,	
	2010	**2009**	**2010**	**2009**
Sales	$ 52,935	$ 42,037	$ 99,515	$ 79,789
Cost of Sales	33,082	25,405	60,329	49,181
Gross Margin	19,853	16,632	39,186	30,608
Operating Expenses:				
Sales and Marketing	10,885	8,975	21,481	16,891
Research and Engineering	2,436	1,850	4,582	3,547
General and Administrative	5,659	6,071	11,617	13,193
Restructuring and Other Operating Charges		(601)		4,222
Total Operating Expenses	18,980	16,295	37,680	37,853
Operating Income (Loss)	**873**	**337**	**1,506**	**(7,245)**
Interest Income	44	53	65	93
Interest Expense	(437)	(474)	(850)	(1,438)
Other Income (Expense), net	104	(150)	396	352
Income (Loss) Before Taxes	**584**	**(234)**	**1,117**	**(8,238)**
Benefit (Provision) for Income Taxes	(804)	923	(1,868)	1,529
Income (Loss) from Continuing Operations	(220)	689	(751)	(6,709)
Income (Loss) from Discontinued Operations, net of Income Tax of $0, $0, $0, and $0	(103)	8	(112)	(1,140)
Net Income (Loss)	**$ (323)**	**$ 697**	**$ (863)**	**$ (7,849)**
Basic and Diluted Income (Loss) Per Share:				
Income (Loss) from Continuing Operations	$ (0.01)	$ 0.02	$ (0.02)	$ (0.17)
Discontinued Operations	0.00	0.00	0.00	(0.02)
Net Income (Loss)	$ (0.01)	$ 0.02	$ (0.02)	$ (0.19)
Weighted Average Shares Used in Computing Basic and Diluted Income (Loss) Per Share:				
Basic	47,160	42,841	47,102	40,295
Diluted	47,160	43,158	47,102	40,295

See Accompanying Notes to Condensed Consolidated Financial Statements

Table of Contents

FLOW INTERNATIONAL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands; unaudited)

	Six Months Ended October 31, 2010	Six Months Ended October 31, 2009
Cash Flows from Operating Activities:		
Net Loss	$ (863)	$ (7,849)
Adjustments to Reconcile Net Loss to Cash Provided by (Used in) Operating Activities:		
Depreciation and Amortization	3,184	2,593
Deferred Income Taxes	947	(1,207)
Provision for Slow Moving and Obsolete Inventory	339	292
Bad Debt Expense	134	447
Warranty Expense	1,377	1,316
Incentive Stock Compensation Expense	1,284	987
Unrealized Foreign Exchange Currency (Gains)	(292)	(53)
Amortization and write off of Deferred Debt Issuance Costs	231	253
OMAX Termination Charge		3,219
Indemnification Charge	112	1,219
Interest Accretion on Subordinated Notes	372	383
Other	12	(455)
Changes in Operating Assets and Liabilities:		
Receivables	(4,245)	(5,973)
Inventories	(4,478)	2,767
Other Operating Assets	702	163
Accounts Payable	(383)	5,887
Accrued Payroll and Related Liabilities	696	(523)
Deferred Revenue and Customer Deposits	1,718	773
Release of Funds from Escrow		17,000
Payment for Patent Litigation Settlement		(15,000)
Payment for OMAX Termination		(2,000)
Other Operating Liabilities	(876)	(3,674)
Net Cash Provided by (Used in) Operating Activities	(29)	565
Cash Flows From Investing Activities:		
Expenditures for Property and Equipment	(800)	(7,545)
Expenditures for Intangible Assets	(349)	(412)
Proceeds from Sale of Property and Equipment	17	4,690
Restricted Cash	(24)	(94)
Net Cash Used in Investing Activities	(1,156)	(3,361)
Cash Flows from Financing Activities:		
Borrowings under Senior Credit Agreement	18,050	5,250
Repayments under Senior Credit Agreement	(16,350)	(18,050)
Repayments Under Other Financing Arrangements	(35)	(1,362)

Repayments of Long Term Obligations		(4,245)
Proceeds from Issuance of Common Stock, net of Issuance Costs		17,439
Payments for Debt Issuance Costs		(607)
Net Cash Provided by (Used In) Financing Activities	1,665	(1,575)
Effect of Changes in Exchange Rates	45	(706)
Net Change in Cash And Cash Equivalents	**525**	**(5,077)**
Cash and Cash Equivalents, Beginning of Period	6,367	10,117
Cash and Cash Equivalents, End of Period	$ 6,892	$ 5,040
Supplemental Disclosures of Cash Flow Information:		
Cash Paid during the Period for:		
Interest	186	860
Income Taxes	411	503
Supplemental Disclosures of Noncash Investing and Financing Activities:		
Accounts Payable Incurred to Acquire Property and Equipment, and Intangible Assets	794	274

See Accompanying Notes to Condensed Consolidated Financial Statements

FLOW INTERNATIONAL CORPORATION
CONDENSED CONSOLIDATED STATEMENT OF SHAREHOLDERS EQUITY
AND COMPREHENSIVE LOSS
(in thousands; unaudited)

	Common Stock Shares	Common Stock Par Value	Capital In Excess of Par	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Shareholders Equity
Balances, April 30, 2009	**37,705**	**$ 372**	**$ 140,634**	**$ (71,403)**	**$ (6,892)**	**$ 62,711**
Components of Comprehensive Loss:						
Net Loss				(7,849)		(7,849)
Adjustment to Minimum Pension Liability, Net of Income Tax of $5					(5)	(5)
Cumulative Translation Adjustment, Net of Income Tax of $207					1,213	1,213
Total Comprehensive Loss						(6,641)
Sale of Common Stock at $2.10 per share, net of Stock Issuance Cost of $1.7 million	8,999	90	17,117			17,207
Stock Compensation	175	3	1,075			1,078
Balances, October 31, 2009	**46,879**	**$ 465**	**$ 158,826**	**$ (79,252)**	**$ (5,684)**	**$ 74,355**
Balances, April 30, 2010	**46,927**	**$ 465**	**$ 159,605**	**$ (79,887)**	**$ (4,559)**	**$ 75,624**
Components of Comprehensive Loss:						
Net Loss				(863)		(863)
Cumulative Translation Adjustment, Net of Income Tax of $3					655	655
Total Comprehensive Loss						(208)
Stock Compensation	241	2	861			863
Balances, October 31, 2010	**47,168**	**$ 467**	**$ 160,466**	**$ (80,750)**	**$ (3,904)**	**$ 76,279**

See Accompanying Notes to Condensed Consolidated Financial Statements

Table of Contents

FLOW INTERNATIONAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(All tabular dollar amounts in thousands, except per share amounts)
(Unaudited)

Note 1: Basis of Presentation

In the opinion of the management of Flow International Corporation (the Company), the accompanying unaudited condensed consolidated financial statements (financial statements) are prepared in accordance with Generally Accepted Accounting Principles (GAAP) for interim financial information and rules and regulations of the Securities and Exchange Commission. Accordingly, certain information and footnote disclosures usually found in financial statements prepared in accordance with GAAP have been condensed or omitted. The unaudited financial statements reflect all adjustments, which in the opinion of management are necessary to fairly state the financial position, results of operations and cash flows for the interim periods presented. These financial statements should be read in conjunction with the audited consolidated financial statements and related notes included in the Company s Annual Report on Form 10-K for the fiscal year ended April 30, 2010.

The preparation of these interim condensed consolidated financial statements requires management to make estimates and judgments that affect the reported amount of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of the Company s financial statements. Operating results for the three and six months ended October 31, 2010 may not be indicative of future results.

Fair Value of Financial Instruments

The carrying value of the Company s current assets and liabilities approximate fair values due to the short-term maturity of these assets and liabilities. Nonfinancial assets and liabilities measured on a nonrecurring basis that are included on the Company s Condensed Consolidated Balance Sheets consist of long-lived assets, including cost-method investments and long-term subordinated notes issued to OMAX that are measured at fair value when impairment indicators exist. Due to significant unobservable inputs, the fair value measures used to evaluate impairment and to calculate a prevailing market interest rate, respectfully, are Level 3 inputs. The carrying amount of these nonfinancial assets and liabilities measured on a nonrecurring basis approximates fair value unless otherwise disclosed in these financial statements.

Reclassification

Certain amounts within the fiscal year 2010 Condensed Consolidated Balance Sheet have been reclassified to conform to the fiscal year 2011 presentation. These reclassifications did not impact total assets or total liabilities of the Company.

Note 2: Recently Issued Accounting Pronouncements

In September 2009, the Financial Accounting Standards Board (FASB) ratified the consensuses reached by the EITF regarding multiple-deliverable revenue arrangements. The new guidance:

- provides principles and application guidance on whether a revenue arrangement contains multiple deliverables, how the arrangement should be separated, and how the arrangement consideration should be allocated;
- requires an entity to allocate revenue in a multiple-deliverable arrangement using estimated selling prices of the deliverables if a vendor does not have vendor-specific objective evidence or third-party evidence of selling price;
- eliminates the use of the residual method and, instead, requires an entity to allocate revenue using the relative selling price method; and
- expands disclosure requirements with respect to multiple-deliverable revenue arrangements.

This new guidance applies to multiple-deliverable revenue arrangements that contain both software and hardware elements, focusing on determining which revenue arrangements are within the scope of software revenue guidance. This new guidance removes tangible products from the scope of the software revenue guidance and provides guidance on determining whether software deliverables in an arrangement that includes a tangible product are within the scope of the software revenue guidance. The accounting guidance should be applied on a prospective basis for revenue arrangements entered into or materially modified in the Company s

fiscal year 2012. Alternatively, an entity can elect to adopt the provisions of these issues on a retrospective basis. The Company is currently assessing the potential impact that the application of the new revenue guidance may have on its consolidated financial statements and disclosures.

Note 3: Receivables, Net

Receivables, net as of October 31, 2010 and April 30, 2010 consisted of the following:

	October 31, 2010	April 30, 2010
Trade Accounts Receivable	$ 26,638	$ 23,717
Unbilled Revenues	14,995	13,184
	41,633	36,901
Less: Allowance for Doubtful Accounts	(1,196)	(1,152)
Receivables, net	$ 40,437	$ 35,749

Unbilled revenues do not contain any amounts which are expected to be collected after one year.

The allowance for doubtful accounts is the Company s best estimate of the amount of probable credit losses on existing receivables. The Company determines the allowance based on historical write-off experience and current economic data. The allowance for doubtful accounts is reviewed quarterly. Past due balances over 90 days and over a specified amount are reviewed individually for collectability. All other balances are reviewed on a pooled basis by type of receivable. Account balances are charged against the allowance when the Company determines that it is probable the receivable will not be recovered.

Note 4: Inventories

Inventories are stated at the lower of cost or market. Costs included in inventories consist of materials, labor and manufacturing overhead, which are related to the purchase or production of inventories. The Company uses the first-in, first-out method or average cost method to determine its cost of inventories. Inventories as of October 31, 2010 and April 30, 2010 consisted of the following:

	October 31, 2010	April 30, 2010
Raw Materials and Parts	$ 15,318	$ 11,895
Work in Process	3,010	2,188
Finished Goods	8,885	8,420
Inventories, net	$ 27,213	$ 22,503

Note 5: Notes Payable

Notes payable as of October 31, 2010 and April 30, 2010 consisted of the following:

	October 31, 2010	April 30, 2010
Senior Credit Facility	$ 2,050	$ 350

The Company has a $40 million secured senior credit facility that expires on June 10, 2011.

Under its current Senior Credit Facility Agreement the Company is required to maintain the following ratios in the current and remaining quarters of fiscal year 2011:

Maximum Consolidated Leverage Ratio (i)	Minimum Fixed Charge Coverage Ratio (ii)

2.50x	2.0x

(i) Defined as the ratio of consolidated indebtedness, excluding the subordinated notes issued to OMAX, to consolidated adjusted Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA) for the most recent four fiscal quarters.

(ii) Defined as the ratio of consolidated adjusted EBITDA, less income taxes and maintenance capital expenditures, during the most recent four quarters to the sum of interest charges during the most recent four quarters and scheduled debt repayments in the next four quarters.

Table of Contents

These covenants also require the Company to meet a liquidity test such that its consolidated indebtedness shall not exceed the total of 65% of the book value of the Company s accounts receivable and 40% of the book value of its inventory.

A violation of any of the covenants above would result in an event of default and accelerate the repayment of all unpaid principal and interest and the termination of any letters of credit. The Company was in compliance with all its financial covenants as of October 31, 2010.

All the Company s domestic assets and certain interests in some foreign subsidiaries are pledged as collateral under its Senior Credit Facility Agreement. Interest on the Line of Credit is based on the bank s prime rate or LIBOR rate plus a percentage spread between 3.25% and 4.5% depending on whether it uses the bank s prime rate or LIBOR rate and based on the Company s current leverage ratio. The Company also pays an annual letter of credit fee equal to 3.5% of the amount available to be drawn under each outstanding stand-by letter of credit. The annual letter of credit fee is payable quarterly in arrears and varies depending on the Company s leverage ratio.

As of October 31, 2010, the Company had $35.8 million available under its Senior Credit Facility, net of $2.1 million in outstanding letters of credit, and $2.1 million in outstanding borrowings. Based on the Company s maximum allowable leverage ratio at the end of the period, the incremental amount it could have borrowed under its Lines of Credit, including the Taiwan credit facilities discussed below, would have been approximately $22.6 million.

Revolving Credit Facilities in Taiwan

There were no outstanding balances under the Company s unsecured Taiwan credit facilities as of October 31, 2010. The unsecured commitment for the Taiwan credit facilities totaled $3.0 million at October 31, 2010, bearing interest at 2.5% per annum.

Note 6: Commitments and Contingencies

Warranty Obligations

The Company s estimated obligations for warranty, which are included as part of Costs of Sales in the Condensed Consolidated Statements of Operations, are accrued concurrently with the revenue recognized. The Company makes provisions for its warranty obligations based upon historical costs incurred for such obligations adjusted, as necessary, for current conditions and factors. Due to the significant uncertainties and judgments involved in estimating the Company s warranty obligations, including changing product designs and specifications, the ultimate amount incurred for warranty costs could change in the near term from the current estimate. The Company believes that its warranty accrual as of October 31, 2010, which is included in the Other Accrued Liabilities line item in the Condensed Consolidated Balance Sheets, is sufficient to cover expected warranty costs.

The following table presents the fiscal year 2011 year-to-date activity for the Company s warranty obligations:

Warranty liability as of May