

HEXCEL CORP /DE/
Form 10-Q
July 23, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the Quarter 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 1-8472

Hexcel Corporation

(Exact name of registrant as specified in its charter)

Delaware 94-1109521
(State of Incorporation) (I.R.S. Employer Identification No.)

Two Stamford Plaza

281 Tresser Boulevard

Stamford, Connecticut 06901-3238

(Address of principal executive offices and zip code)

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Registrant's telephone number, including area code: (203) 969-0666

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	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 by Rule 12b-2 of the Exchange Act). Yes No

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

Class	Outstanding at July 16, 2018
COMMON STOCK	87,519,465

HEXCEL CORPORATION AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION

ITEM 1. Condensed Consolidated Financial Statements

Hexcel Corporation and Subsidiaries
Condensed Consolidated Balance Sheets

	(Unaudited)	
	June 30,	December
(In millions)	2018	31, 2017
Assets		
Current assets:		
Cash and cash equivalents	\$39.1	\$ 60.1
Accounts receivable, net	287.2	248.7
Inventories, net	305.4	314.0
Contract assets	37.7	
Prepaid expenses and other current assets	38.4	33.9
Total current assets	707.8	656.7
Property, plant and equipment	2,800.1	2,743.9
Less accumulated depreciation	(920.5)	(877.6)
Net property, plant and equipment	1,879.6	1,866.3
Goodwill and other intangible assets	145.3	148.7
Investments in affiliated companies	44.6	47.7
Other assets	58.8	61.5
Total assets	\$2,836.1	\$ 2,780.9
Liabilities and Stockholders' Equity		
Current liabilities:		
Current portion of debt	\$9.3	\$ 4.3
Accounts payable	147.1	144.1
Accrued compensation and benefits	68.8	73.0
Accrued liabilities	68.6	40.7
Total current liabilities	293.8	262.1
Commitments and contingencies (see Note 13)		
Long-term debt	930.1	805.6
Retirement obligations	41.3	45.4
Other non-current liabilities	171.1	172.7
Total liabilities	1,436.3	1,285.8
Stockholders' equity:		
Common stock, \$0.01 par value, 200.0 shares authorized, 108.4 shares and 107.8 shares issued at June 30, 2018 and December 31, 2017, respectively	1.1	1.1

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Additional paid-in capital	792.0	774.3
Retained earnings	1,606.2	1,496.1
Accumulated other comprehensive loss	(80.8)	(45.0)
	2,318.5	2,226.5
Less – Treasury stock, at cost, 20.9 shares at June 30, 2018, and 18.2 shares		
at December 31, 2017, respectively.	(918.7)	(731.4)
Total stockholders' equity	1,399.8	1,495.1
Total liabilities and stockholders' equity	\$2,836.1	\$2,780.9

The accompanying notes are an integral part of these condensed consolidated financial statements.

Hexcel Corporation and Subsidiaries

Condensed Consolidated Statements of Operations

(In millions, except per share data)	(Unaudited) Quarter Ended		(Unaudited) Six Months	
	June 30, 2018	2017	2018	2017
Net sales	\$547.5	\$491.3	\$1,087.6	\$970.1
Cost of sales	402.7	351.4	800.2	696.1
Gross margin	144.8	139.9	287.4	274.0
Selling, general and administrative expenses	35.3	38.1	81.7	81.0
Research and technology expenses	13.0	12.1	26.8	24.7
Other operating income (expense)	-	-	-	-
Operating income	96.5	89.7	178.9	168.3
Interest expense, net	8.7	6.8	16.7	13.0
Income before income taxes, and equity in earnings from affiliated companies	87.8	82.9	162.2	155.3
Provision for income taxes	20.0	22.1	34.1	30.7
Income before equity in earnings from affiliated companies	67.8	60.8	128.1	124.6
Equity in earnings from affiliated companies	1.0	0.8	2.3	1.6
Net income	\$68.8	\$61.6	\$130.4	\$126.2
Basic net income per common share	\$0.77	\$0.68	\$1.45	\$1.39
Diluted net income per common share	\$0.76	\$0.67	\$1.44	\$1.37
Dividends per share	\$0.125	\$0.11	\$0.25	\$0.22
Weighted-average common shares:				
Basic	88.8	90.7	89.4	91.1
Diluted	89.9	92.0	90.5	92.4

Hexcel Corporation and Subsidiaries

Condensed Consolidated Statements of Comprehensive Income

(In millions)	(Unaudited) Quarter Ended		(Unaudited) Six Months	
	June 30, 2018	2017	2018	2017
Net Income	\$68.8	\$61.6	\$130.4	\$126.2
Currency translation adjustments	(57.4)	49.4	(25.8)	58.5
Net unrealized gains (losses) on pension and other retirement benefits	1.3	(0.8)	0.5	(1.0)
Net unrealized (losses) gains on financial instruments (net of tax)	(16.9)	16.5	(12.1)	23.9
Total other comprehensive income	(73.0)	65.1	(37.4)	81.4

Comprehensive (loss) income	\$ (4.2)	\$ 126.7	\$ 93.0	\$ 207.6
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The accompanying notes are an integral part of these condensed consolidated financial statements.

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Hexcel Corporation and Subsidiaries

Condensed Consolidated Statements of Cash Flows

(In millions)	(Unaudited)	
	Six Months	
	Ended June 30,	
	2018	2017
Cash flows from operating activities		
Net income	\$ 130.4	\$ 126.2
Reconciliation to net cash provided by operating activities:		
Depreciation and amortization	59.6	49.5
Amortization related to financing	0.7	0.4
Deferred income taxes	12.7	2.0
Equity in earnings from affiliated companies	(2.3)	(1.6)
Stock-based compensation	12.0	13.3
Changes in assets and liabilities:		
(Increase) decrease in accounts receivable	(43.4)	2.4
Increase in inventories	(28.6)	(11.6)
Increase in prepaid expenses and other current assets	(12.9)	(2.9)
Increase in accounts payable/accrued liabilities	24.7	5.0
Other – net	4.3	(0.3)
Net cash provided by operating activities	157.2	182.4
Cash flows from investing activities		
Capital expenditures	(101.9)	(169.2)
Acquisition of business and investment in affiliate		(10.0)
Net cash used for investing activities	(101.9)	(179.2)
Cash flows from financing activities		
Proceeds from senior notes due 2027 (including original issue discount of \$1.7)		398.3
Issuance costs related to senior notes due 2027		(3.7)
Proceeds from settlement of treasury locks associated with senior notes due 2027		10.0
Proceeds from Euro term loan		37.4
Repayments of Euro term loan	(4.2)	(4.1)
Borrowing from senior unsecured credit facility	379.0	252.0
Repayment of senior unsecured credit facility	(244.0)	(552.0)
Repayment of capital lease obligation and other debt, net		0.2
Dividends paid	(22.4)	(20.1)
Repurchase of stock	(181.0)	(120.8)
Activity under stock plans	(0.7)	5.6
Net cash (used for) provided by financing activities	(73.3)	2.8
Effect of exchange rate changes on cash and cash equivalents	(3.0)	4.3
Net (decrease) increase in cash and cash equivalents	(21.0)	10.3
Cash and cash equivalents at beginning of period	60.1	35.2
Cash and cash equivalents at end of period	\$ 39.1	\$ 45.5
Supplemental data:		

Accrual basis additions to property, plant and equipment	\$90.0	\$170.1
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The accompanying notes are an integral part of these condensed consolidated financial statements.

HEXCEL CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1 — Significant Accounting Policies

In these notes, the terms “Hexcel,” “the Company,” “we,” “us,” or “our” mean Hexcel Corporation and subsidiary companies. The accompanying Condensed Consolidated Financial statements are those of Hexcel Corporation. Refer to Note 1 to the consolidated financial statements included in the Annual Report on Form 10-K for the year ended December 31, 2017 for a discussion of our significant accounting policies. Significant changes to our accounting policies subsequent to the filing of our Form 10-K, relate solely to the adoption of Topic 606, Revenue from Contracts with Customers, are discussed below in Recent Accounting Pronouncements as well as in Note 9.

Basis of Presentation

The accompanying Condensed Consolidated Financial Statements have been prepared from the unaudited accounting records of Hexcel pursuant to rules and regulations of the Securities and Exchange Commission (“SEC”) and in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial information. Certain information and footnote disclosures normally included in financial statements have been omitted pursuant to rules and regulations of the SEC. In the opinion of management, the Condensed Consolidated Financial Statements include all normal recurring adjustments as well as any non-recurring adjustments necessary to present fairly the statement of financial position, results of operations and cash flows for the interim periods presented. The Condensed Consolidated Balance Sheet as of December 31, 2017 was derived from the audited 2017 consolidated balance sheet. Interim results are not necessarily indicative of results expected for any other interim period or for the full year. These consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in our 2017 Annual Report on Form 10-K. Within the Unaudited Condensed Consolidated Statement of Cash Flows for the six months ended June 30, 2017, borrowings and repayments related to our revolving credit facility previously presented net within financing activities have been presented gross to conform to the current year presentation.

Investments in Affiliated Companies

At June 30, 2018, we had a 50% equity investment in Aerospace Composites Malaysia Sdn. Bhd. (“ACM”). This investment is accounted for using the equity method of accounting.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standard Update No. 2014-09 (ASU 2014-09), Revenue from Contracts with Customers (“ASC 606”). The update clarified the principles for recognizing revenue and developed a common revenue standard for all industries. We adopted this new standard January 1, 2018, using the modified retrospective method. As a result of adopting this guidance under the modified

retrospective method we adjusted the opening balance of our retained earnings by approximately \$3.8 million, which represented the cumulative net earnings effect of revenue recognized over time prior to the date of adoption, related to those contracts whose performance obligations were not fully satisfied by the adoption date.

In February 2016, the FASB issued Accounting Standards Update No. 2016-02 (ASU 2016-02), Leases (Topic 842). This ASU requires lessees to recognize a right of use asset and lease liability on the balance sheet for all leases, with the exception of short-term leases. The Company will adopt this standard on January 1, 2019. We are in the process of assessing the impact this new standard will have on our financial statements. We will adopt the provisions of this standard using the modified retrospective method which allows companies to recognize existing leases at the adoption date regardless of when they were entered into.

In March 2017, the FASB issued Accounting Standards Update No. 2017-07 (ASU 2017-07), Compensation-Retirement Benefits, that amends the presentation of net periodic pension cost and net periodic postretirement benefit cost. This amendment requires entities to disaggregate the service cost component from the other components of net periodic benefit cost, to report the service cost component in the same line item as other compensation costs and to report the other components of net periodic benefit cost separately as a line item below operating income on our statement of operations. In addition, capitalization of net periodic benefit cost in assets is limited to the service cost component. We adopted this amendment on January 1, 2018. The adoption did not have a material impact to our financial statements or disclosures.

In August 2017, the FASB issued Accounting Standards Update No. 2017-12 (ASU 2017-12), Targeted Improvement to Accounting for Hedging Activities, which better aligns hedge accounting with an organization's risk management activities in the financial statements. In addition, the standard simplified the application of hedge accounting guidance in areas where practice issues exist. We adopted this standard on January 1, 2018, with no material impact to our results of operations, or financial position.

In February 2018, the FASB issued Accounting Standards Update No. 2018-02 (ASU 2018-02), Income Statement—Reporting Comprehensive Income (Topic 220), which amends the previous guidance to allow for certain tax effects “stranded” in accumulated other comprehensive income, which are impacted by the Tax Cuts and Jobs Act (the “Act”), to be reclassified from accumulated other comprehensive income into retained earnings. This amendment pertains only to those items impacted by the new tax law and will not apply to any future tax effects stranded in accumulated other comprehensive income. This standard is effective for fiscal years beginning after December 15, 2018, and allows for early adoption. The Company elected to early adopt this standard during the quarter ended March 31, 2018. As a result of the adoption of this standard, the Company reduced the opening balance of retained earnings by approximately \$1.6 million.

Note 2 — Net Income per Common Share

(In millions, except per share data)	Quarter		Six Months	
	Ended June 30, 2018	2017	Ended June 30, 2018	2017
Basic net income per common share:				
Net income	\$68.8	\$61.6	\$130.4	\$126.2
Weighted average common shares outstanding	88.8	90.7	89.4	91.1
Basic net income per common share	\$0.77	\$0.68	\$1.45	\$1.39
Diluted net income per common share:				
Net income	68.8	61.6	130.4	126.2
Weighted average common shares outstanding — Basic	88.8	90.7	89.4	91.1
Plus incremental shares from assumed conversions:				
Restricted stock units	0.4	0.4	0.4	0.4
Stock options	0.7	0.9	0.7	0.9
Weighted average common shares outstanding — Dilutive	89.9	92.0	90.5	92.4
Diluted net income per common share	\$0.76	\$0.67	\$1.44	\$1.37

Total shares underlying stock options of 0.1 million were excluded from the computation of diluted net income per share for both the three and six months ended June 30, 2018, as they were anti-dilutive. Total shares underlying stock options of 0.1 million and 0.2 million, respectively, were excluded from the computation of diluted net income per share for the three and six months ended June 30, 2017, as they were anti-dilutive.

Note 3 — Inventories

	June 30,	December
(In millions)	2018	2017
Raw materials	\$ 137.0	\$ 126.7
Work in progress	49.6	52.1
Finished goods	118.8	135.2
Total Inventory	\$ 305.4	\$ 314.0

Note 4 — Retirement and Other Postretirement Benefit Plans

We maintain qualified and nonqualified defined benefit retirement plans covering certain current and former U.S. and European employees, retirement savings plans covering eligible U.S. and U.K. employees and certain postretirement health care and life insurance benefit plans covering eligible U.S. retirees. We also participate in a union sponsored multi-employer pension plan covering certain U.S. employees with union affiliations.

Defined Benefit Retirement Plans

Net Periodic Benefit Costs

Net periodic benefit costs of our defined benefit retirement plans for the three and six months ended June 30, 2018 and 2017 were as follows:

(In millions)	Quarter Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
U.S. Nonqualified Defined Benefit Retirement Plans				
Service cost	\$0.3	\$0.4	\$0.6	\$0.7
Interest cost	0.2	0.1	0.3	0.3
Settlement expense		0.1		0.1
Net amortization and deferral		0.1		0.2
Net periodic benefit cost	\$0.5	\$0.7	\$0.9	\$1.3

(In millions)	June 30, 2018	December 31, 2017
Amounts recognized on the balance sheet:		
Accrued liabilities	\$ 4.8	\$ 4.5
Other non-current liabilities		