Thermon Group Holdings, Inc.
Form 10-Q
February 04, 2016

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 December 31, 2015

OR

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

Commission File Number: 001-35159

THERMON GROUP HOLDINGS, INC.
(Exact name of registrant as specified in its charter)

Delaware	27-2228185
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

100 Thermon Drive, San Marcos, Texas 78666
(Address of principal executive offices)

(512) 396-5801
(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. xYes oNo

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). xYes o 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.

Large accelerated filer x	Accelerated filer o
Non-accelerated filer o	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).
oYes x No

As of February 1, 2016, the registrant had 32,215,894 shares of common stock, par value $0.001 per share, outstanding.

THERMON GROUP HOLDINGS, INC.

QUARTERLY REPORT
FOR THE QUARTER ENDED DECEMBER 31, 2015

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Condensed Consolidated Balance Sheets
(Dollars in Thousands, except share and per share data)

	December 31, 2015 (Unaudited)	March 31, 2015
Assets		
Current assets:		
Cash and cash equivalents	$79,101	$93,774
Accounts receivable, net of allowance for doubtful accounts of $748 and $785 as of December 31, 2015 and March 31, 2015, respectively	52,958	60,441
Inventories, net	44,098	41,008
Costs and estimated earnings in excess of billings on uncompleted contracts	7,934	6,804
Prepaid expenses and other current assets	8,344	5,128
Deferred income taxes	3,290	3,549
Total current assets	195,725	210,704
Property, plant and equipment, net	39,963	34,824
Goodwill	120,460	105,232
Intangible assets, net	105,043	100,813
Debt issuance costs, net	1,074	1,358
Other long term assets	349	378
Total assets	$462,614	$453,309
Liabilities		
Current liabilities:		
Accounts payable	$19,169	$17,145
Accrued liabilities	13,107	17,417
Current portion of long term debt	13,500	13,500
Borrowings under revolving credit facility	5,000	—
Billings in excess of costs and estimated earnings on uncompleted contracts	3,223	2,366
Income taxes payable	2,816	2,710
Total current liabilities	56,815	53,138
Long-term debt, net of current maturities	84,375	94,500
Deferred income taxes	34,061	30,835
Other non-current liabilities	3,046	3,070
Total liabilities	178,297	181,543
Equity		
Common stock: $.001 par value; 150,000,000 authorized; 32,210,938 and 32,082,393 shares issued and outstanding at December 31, 2015 and March 31, 2015, respectively	32	32
Preferred stock: $.001 par value; 10,000,000 authorized; no shares issued and outstanding	—	—
Additional paid in capital	215,726	213,885
Accumulated other comprehensive loss	(54,501)	(41,400)
Retained earnings	119,054	99,249
Total Thermon Group Holdings, Inc. shareholders' equity	280,311	271,766
Non-controlling interests	4,006	—
Total equity	284,317	271,766

Total liabilities and equity	$462,614	$453,309

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

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Thermon Group Holdings, Inc.

Condensed Consolidated Statements of Operations and Comprehensive Income (Unaudited)
(Dollars in Thousands, except share and per share data)

	Three Months Ended December 31, 2015	Three Months Ended December 31, 2014	Nine Months Ended December 31, 2015	Nine Months Ended December 31, 2014
Sales	$74,427	$87,622	$209,584	$234,322
Cost of sales	39,298	42,089	110,364	113,723
Gross profit	35,129	45,533	99,220	120,599
Operating expenses:				
Marketing, general and administrative and engineering	20,167	19,631	59,021	57,973
Amortization of intangible assets	3,135	2,683	8,979	8,175
Income from operations	11,827	23,219	31,220	54,451
Other income/(expenses):				
Interest income	91	138	309	365
Interest expense	(918)	(1,094)	(3,227)	(3,580)
Other expense	(377)	(496)	(664)	(1,334)
Income before provision for income taxes	10,623	21,767	27,638	49,902
Income tax expense	1,954	6,164	7,462	11,017
Net income	$8,669	$15,603	$20,176	$38,885
Income attributable to non-controlling interests	189	—	371	—
Net income available to Thermon Group Holdings, Inc.	$8,480	$15,603	$19,805	$38,885
Comprehensive income:				
Net income available to Thermon Group Holdings, Inc.	$8,480	$15,603	$19,805	$38,885
Foreign currency translation adjustment	(6,047)	(8,628)	(13,337)	(15,480)
Derivative valuation, net of tax	373	(202)	237	(51)
Comprehensive income	$2,806	$6,773	$6,705	$23,354
Net Income per common share:				
Basic	$0.26	$0.49	$0.62	$1.21
Diluted	0.26	0.48	0.61	1.20
Weighted-average shares used in computing net income per common share:				
Basic	32,210,081	32,066,877	32,162,800	32,014,840
Diluted	32,596,747	32,455,463	32,575,757	32,391,110

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

Thermon Group Holdings, Inc.

Condensed Consolidated Statements of Cash Flows (Unaudited)
(Dollars in Thousands)

	Nine Months Ended December 31, 2015	Nine Months Ended December 31, 2014
Operating activities		
Net income	$20,176	$38,885
Adjustment to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	12,971	10,679
Amortization of deferred debt issuance costs	629	350
Stock compensation expense	2,764	2,302
Deferred income taxes	(1,658)	(5,818)
Other	939	1,496
Changes in operating assets and liabilities:		
Accounts receivable	10,806	(18,223)
Inventories	(3,183)	(8,952)
Costs and estimated earnings in excess of billings on uncompleted contracts	(952)	(1,317)
Other current and noncurrent assets	(1,627)	(1,223)
Accounts payable	954	4,394
Accrued liabilities and noncurrent liabilities	(4,266)	5,106
Income taxes payable and receivable	(2,505)	6,408
Net cash provided by operating activities	35,048	34,087
Investing activities		
Purchases of property, plant and equipment	(9,464)	(4,148)
Sale of rental equipment at net book value	1,726	—
Cash paid for acquisitions (net of cash acquired)	(31,180)	—
Net cash used in investing activities	(38,918)	(4,148)
Financing activities		
Proceeds from revolving credit facility	5,000	—
Payments on long term debt	(10,125)	(10,125)
Issuance costs associated with revolving line of credit and long term debt	(341)	(290)
Proceeds from exercise of stock options	204	484
Repurchase of employee stock units on vesting	(1,265)	—
Benefit from excess tax deduction from option exercises	133	1,450
Lease financing	(148)	(156)
Net cash used in financing activities	(6,542)	(8,637)
Effect of exchange rate changes on cash and cash equivalents	(4,261)	(3,654)
Change in cash and cash equivalents	(14,673)	17,648
Cash and cash equivalents at beginning of period	93,774	72,640
Cash and cash equivalents at end of period	$79,101	$90,288

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

Thermon Group Holdings, Inc.

Notes to Condensed Consolidated Financial Statements (Unaudited)
(Dollars in Thousands, Except Share and Per Share Data)

1. Basis of Presentation and Accounting Policy Information

Thermon Group Holdings, Inc. and its direct and indirect subsidiaries are referred to collectively as “we,” “our,” or the “Company” herein. We are a provider of highly engineered thermal solutions for process industries. Our thermal solutions, also referred to as heat tracing, provide an external heat source to pipes, vessels and instruments for the purposes of freeze protection, temperature and flow maintenance, environmental monitoring, and surface snow and ice melting. As a manufacturer, we provide a suite of products (heating cables, tubing bundles and control systems) and services (design optimization, engineering, installation and maintenance services) required to deliver comprehensive solutions to complex projects.
The accompanying unaudited condensed consolidated financial statements should be read in conjunction with our audited consolidated financial statements and notes thereto for the year ended March 31, 2015. In our opinion, the accompanying consolidated financial statements reflect all adjustments (consisting only of normal recurring items) considered necessary to present fairly our financial position at December 31, 2015 and March 31, 2015, and the results of our operations for the three and nine months ended December 31, 2015 and 2014.
Use of Estimates
Generally accepted accounting principles (“GAAP”) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. While our management has based their assumptions and estimates on the facts and circumstances existing at December 31, 2015, actual results could differ from those estimates and affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities and the corresponding revenues and expenses as of the date of the financial statements. The operating results for the three and nine months ended December 31, 2015 are not necessarily indicative of the results that may be achieved for the fiscal year ending March 31, 2016.

Correction of an error

During the three months ended June 30, 2015, the Company recorded a correction of an error that reduced marketing, general and administrative and engineering expense by $498 and decreased additional paid in capital by an equivalent amount. In previous years, the Company had expensed the withholding tax value of equity awards that were withheld by the Company at vesting. The Company determined that the value of withheld shares should have been recorded as a reduction to additional paid in capital.

Recent Accounting Pronouncements
Revenue Recognition - In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update No. 2014-09 “Revenue from Contracts with Customers” (Topic 606), which amends the existing revenue recognition requirements and guidance. Under the new guidance, revenue is recognized when promised goods or services are transferred to customers in an amount that reflects the consideration that is expected to be received for those goods or services. The new revenue standard may be applied retrospectively to each prior period presented or retrospectively with the cumulative effect recognized as of the date of adoption. The Company will adopt the standard on April 1, 2018. We have not selected a transition method and we are currently evaluating the effect that the updated standard will have on our consolidated financial statements and related disclosures.

Stock Compensation - In June 2014, the Financial Accounting Standards Board issued Accounting Standards Update No. 2014-12 (Topic 718), which clarified the treatment of share-based payments when a performance target could be achieved after the requisite service period. Under the new guidance, compensation cost should be recognized over the requisite service period when it becomes probable that the performance target will be achieved. The total compensation cost recognized should reflect the number of awards that are expected to vest and should be adjusted to reflect those awards that ultimately vest. We adopted this standard April 1, 2015 and it did not have a material impact on our condensed consolidated financial statements.

Interest- In April 2015, the Financial Accounting Standards Board issued Accounting Standards Update 2015-3 "Interest-Imputation of Interest" (Subtopic 835-30). The new guidance changes the presentation of debt issuance costs in financial statements and specifies that debt issuance costs related to a note shall be reported in the balance sheet as a direct deduction from the associated face amount of the note. The guidance does not change the current guidance related to the recognition and measurement of debt issuance costs. The amortization of debt issuance costs will continue to be reported as interest expense. The guidance is effective for years and interim periods within those fiscal years beginning after December 15, 2015. Early adoption is allowed for all entities and the new guidance shall be applied to all prior periods retrospectively. We are currently evaluating when to adopt this ASU. If the standard update were adopted as of December 31, 2015, our outstanding debt obligations would have been reduced by $986 and $1,217 as of December 31, 2015 and March 31, 2015, respectively. The adoption of this guidance will have no impact on the presentation of our condensed consolidated statements of operations.

Interest- In August 2015, the Financial Accounting Standards Board issued Accounting Standards Update 2015-15 "Imputation of Interest" (Subtopic 835-30). The guidance clarified the treatment of the presentation of debt issuance costs associated with a revolving line of credit. Under the guidance these costs can continue to be reported as an asset. As there were no changes to the pre-existing guidance the standard is considered to be effective immediately and had no impact on our condensed consolidated financial statements.

Inventory- In July 2015, the Financial Accounting Standards Board issued Accounting Standards Update 2015-11 "Simplifying the Measurement of Inventory" (Topic 330). Under the new guidance, inventory is measured at the lower of cost and net realizable value, and the new guidance eliminates the use of replacement cost and net realizable value less a normal profit margin as techniques to value inventory. Net realizable value is defined as the estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. The new guidance will be applied prospectively for annual periods and interim periods within fiscal years beginning after December 15, 2016. We do not anticipate the adoption of this standard will have a material impact on our condensed consolidated financial statements.

Business Combinations- In September 2015, the Financial Accounting Standards Board issued Accounting Standards Update 2015-16 "Simplifying the Accounting for Measurement-Period Adjustments" (Topic 805). Under the new guidance, an acquirer must recognize adjustments to provisional amounts that are identified in the reporting period in which the adjustments amounts are determined. Companies are required to disclose the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustments to the provisional amounts had been recognized as of the acquisition date. The new guidance is to be applied prospectively for fiscal years beginning after December 15, 2015 and interim periods within those fiscal years. Early adoption is permitted. We adopted this standard in September 2015 and it did not have a material impact on our condensed consolidated financial statements.

Income Taxes- In November 2015, the Financial Accounting Standards Board issued Accounting Standards Update 2015-17, which requires an entity to present all deferred income tax assets and liabilities as noncurrent. Under the previous guidance, an entity had to classify deferred income tax assets and liabilities into current and noncurrent based on the classification of the related asset or liability. The new guidance is effective for annual periods beginning after December 15, 2016 and interim periods within those years. Early adoption is permitted. In the year of adoption, the guidance can be applied either prospectively or retrospectively. We are currently evaluating when to adopt the standard and the impact on our condensed consolidated balance sheet. The adoption of this guidance will have no impact on the presentation of our condensed consolidated statements of operations or condensed consolidated statements of cash flows.

Financial Instruments- In January 2016, the Financial Accounting Standards Board issued Accounting Standards Update 2016-01, which amends the guidance on the classification and measurement of financial instruments. The amendment requires all equity investments to be measured at fair value with changes in the fair value recognized through earnings. The amendment also requires 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 credit risk when an entity has elected the fair value option. The guidance eliminates the requirement to disclose the methods and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet. The new guidance is effective for fiscal years and interim periods within those fiscal years beginning after December 15, 2017. Early adoption is permitted for certain provisions of the accounting standards update. Upon the adoption of the standard, an entity will be required to make a cumulative-effect adjustment to retained earnings as of the beginning of such reporting period. We are currently evaluating when to adopt this standard. Upon adoption, we do not anticipate this standard will have a material impact on our condensed consolidated financial statements.

2. Fair Value Measurements

Fair Value. We measure fair value based on authoritative accounting guidance, which defines fair value, establishes a framework for measuring fair value and expands on required disclosures regarding fair value measurements.

Inputs are referred to as assumptions that market participants would use in pricing the asset or liability. The uses of inputs in the valuation process are categorized into a three-level fair value hierarchy.

- Level 1 — uses quoted prices in active markets for identical assets or liabilities we have the ability to access.
- Level 2 — uses observable inputs other than quoted prices in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.
- Level 3 — uses one or more significant inputs that are unobservable and supported by little or no market activity, and that reflect the use of significant management judgment.

Financial assets and liabilities with carrying amounts approximating fair value include cash, trade accounts receivable, accounts payable, accrued expenses and other current liabilities. The carrying amount of these financial assets and liabilities approximates fair value because of their short maturities. At December 31, 2015 and March 31, 2015, no assets or liabilities were valued using Level 3 criteria.

Information about our long-term debt that is not measured at fair value is as follows:

	December 31, 2015		March 31, 2015		
	Carrying Value	Fair Value	Carrying Value	Fair Value	Valuation Technique
Financial Liabilities					
Long-term debt	$97,875	$97,875	$108,000	$108,000	Level 2 - Market Approach
Revolving credit facility	$5,000	$5,000	—	—	Level 2 - Market Approach

At December 31, 2015 and March 31, 2015, the fair value of our variable rate term loan and revolving credit facility approximates its carrying value as we pay interest based on the current market rate. As the quoted price is only available for similar financial assets, the Company concluded the pricing is indire