

MERCER INTERNATIONAL INC.
Form 10-Q
April 28, 2016

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 quarterly period ended March 31, 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 No.: 000-51826

MERCER INTERNATIONAL INC.

(Exact name of Registrant as specified in its charter)

Washington
(State or other jurisdiction)

47-0956945
(I.R.S. Employer Identification No.)

(of incorporation or organization)

Suite 1120, 700 West Pender Street, Vancouver, British Columbia, Canada, V6C 1G8

(Address of office)

(604) 684-1099

(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. 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 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, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer Accelerated Filer Non-Accelerated Filer Smaller Reporting Company
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES NO

The Registrant had 64,656,138 shares of common stock outstanding as at April 27, 2016.

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

MERCER INTERNATIONAL INC.

INTERIM CONSOLIDATED FINANCIAL STATEMENTS

FOR THE THREE MONTHS ENDED MARCH 31, 2016

(Unaudited)

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MERCER INTERNATIONAL INC.**INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS****(Unaudited)****(In thousands of U.S. dollars, except per share data)**

	Three Months Ended March 31,	
	2016	2015
Revenues		
Pulp	\$ 230,629	\$ 234,657
Energy and chemicals	23,214	22,890
	253,843	257,547
Costs and expenses		
Operating costs, excluding depreciation and amortization	196,942	184,948
Operating depreciation and amortization	17,032	17,304
Selling, general and administrative expenses	11,769	11,364
Operating income	28,100	43,931
Other income (expense)		
Interest expense	(13,191)	(13,884)
Foreign exchange gain (loss) on intercompany debt	555	(6,610)
Loss on derivative instruments (Note 9)	(210)	(524)
Other expense	(286)	(14)
Total other expense	(13,132)	(21,032)
Income before provision for income taxes	14,968	22,899
Current income tax provision	(1,753)	(3,352)
Deferred income tax provision	(4,446)	(5,913)
Net income	\$ 8,769	\$ 13,634
Net income per common share (Note 7)		
Basic and diluted	\$ 0.14	\$ 0.21
Cash dividend declared per common share (Note 6)	\$ 0.115	\$ -

INTERIM CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**(Unaudited)****(In thousands of U.S. dollars)**

	Three Months Ended March 31,	
	2016	2015
Net income	\$ 8,769	\$ 13,634
Other comprehensive income (loss), net of taxes		
Foreign currency translation adjustment (net of tax effect of \$nil in all periods)	52,336	(111,805)
Change in unrecognized losses and prior service costs related to defined benefit plans (net of tax effect of \$nil in all periods)	290	248
Change in unrealized gains/losses on marketable securities (net of tax effect of \$nil in all periods)	(2)	(71)
Other comprehensive income (loss), net of taxes	52,624	(111,628)
Comprehensive income (loss)	\$ 61,393	\$ (97,994)

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

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MERCER INTERNATIONAL INC.**INTERIM CONSOLIDATED BALANCE SHEETS****(Unaudited)****(In thousands of U.S. dollars, except share and per share data)**

	March 31, 2016	December 31, 2015
ASSETS		
Current assets		
Cash and cash equivalents	\$ 129,869	\$ 99,629
Restricted cash (Note 9)	9,682	9,230
Accounts receivable	137,344	134,254
Inventories (Note 2)	133,688	141,001
Prepaid expenses and other	5,411	4,697
Total current assets	415,994	388,811
Property, plant and equipment, net	791,893	762,391
Intangible and other assets	9,333	8,461
Deferred income tax	21,244	23,154
Total assets	\$ 1,238,464	\$ 1,182,817
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities		
Accounts payable and other (Note 3)	\$ 122,044	\$ 103,450
Pension and other post-retirement benefit obligations (Note 5)	1,036	971
Total current liabilities	123,080	104,421
Debt (Note 4)	615,966	638,043
Interest rate derivative liability (Note 9)	7,008	6,533
Pension and other post-retirement benefit obligations (Note 5)	26,916	25,374
Capital leases and other	12,304	12,299
Deferred income tax	15,365	13,171
Total liabilities	800,639	799,841
Shareholders' equity		
Common shares \$1 par value; 200,000,000 authorized; 64,656,000 issued and outstanding (2015 - 64,502,000)	64,618	64,424
Additional paid-in capital	329,943	329,246

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Retained earnings (Note 6)	162,214	160,880
Accumulated other comprehensive loss (Note 8)	(118,950)	(171,574)
Total shareholders' equity	437,825	382,976
Total liabilities and shareholders' equity	\$ 1,238,464	\$ 1,182,817
Commitments and contingencies (Note 11)		
Subsequent event (Note 6)		

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

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MERCER INTERNATIONAL INC.**INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited)****(In thousands of U.S. dollars)**

	Three Months Ended March 31,	
	2016	2015
Cash flows from (used in) operating activities		
Net income	\$ 8,769	\$ 13,634
Adjustments to reconcile net income to cash flows from operating activities		
Unrealized loss on derivative instruments	210	524
Depreciation and amortization	17,219	17,387
Deferred income taxes	4,446	5,913
Foreign exchange (gain) loss on intercompany debt	(555)	6,610
Defined benefit pension plan and other post-retirement benefit plan expense	476	709
Stock compensation expense	891	630
Other	1,016	456
Defined benefit pension plan and other post-retirement benefit plan contributions	(426)	(475)
Changes in working capital		
Accounts receivable	3,953	(9,621)
Inventories	14,636	(4,921)
Accounts payable and accrued expenses	13,210	27,773
Other	(379)	1,226
Net cash from (used in) operating activities	63,466	59,845
Cash flows from (used in) investing activities		
Purchase of property, plant and equipment	(6,936)	(7,064)
Purchase of intangible assets	(520)	(873)
Other	(102)	222
Net cash from (used in) investing activities	(7,558)	(7,715)
Cash flows from (used in) financing activities		
Repurchase of notes	(23,079)	-
Dividend payment	(7,418)	-
Proceeds from (repayment of) revolving credit facilities, net	-	953
Other	(486)	(218)
Net cash from (used in) financing activities	(30,983)	735

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Effect of exchange rate changes on cash and cash equivalents	5,315	(6,194)
Net increase in cash and cash equivalents	30,240	46,671
Cash and cash equivalents, beginning of period	99,629	53,172
Cash and cash equivalents, end of period	\$ 129,869	\$ 99,843
Supplemental cash flow disclosure		
Cash paid for interest	\$ 599	\$ 126
Cash paid for income taxes	\$ 4,630	\$ 413

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

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MERCER INTERNATIONAL INC.

NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(In thousands of U.S. dollars, except share and per share data)

Note 1. The Company and Summary of Significant Accounting Policies

Nature of Operations and Basis of Presentation

The interim consolidated financial statements contained herein include the accounts of Mercer International Inc. (Mercer Inc.) and all of its subsidiaries (collectively the Company). The Company s shares of common stock are quoted and listed for trading on both the NASDAQ Global Market and the Toronto Stock Exchange.

The interim consolidated financial statements have been prepared by the Company pursuant to the rules and regulations of the United States Securities and Exchange Commission (the SEC). The year-end Consolidated Balance Sheet data was derived from audited financial statements. The footnote disclosure included herein has been prepared in accordance with accounting principles generally accepted for interim financial statements in the United States (GAAP). The interim consolidated financial statements should be read together with the audited consolidated financial statements and accompanying notes included in the Company s latest annual report on Form 10-K for the fiscal year ended December 31, 2015. In the opinion of the Company, the unaudited interim consolidated financial statements contained herein contain all adjustments necessary for a fair statement of the results of the interim periods included. The results for the periods included herein may not be indicative of the results for the entire year.

The Company has three pulp mills that are aggregated into one reportable business segment, market pulp. Accordingly, the results presented are those of the reportable business segment.

In these interim consolidated financial statements, unless otherwise indicated, all amounts are expressed in United States dollars (U.S. dollars or \$). The symbol € refers to euros and the symbol C\$ refers to Canadian dollars.

Use of Estimates

Preparation of financial statements and related disclosures in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Significant management judgment is required in determining the accounting for, among other things, pensions and other post-retirement benefit obligations, deferred income taxes (valuation allowance and permanent reinvestment), depreciation and amortization, future cash flows associated with impairment testing for long-lived assets, legal liabilities and contingencies. Actual results could differ materially from these estimates, and changes in these estimates are recorded when known.

New Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update 2014-9, Revenue Recognition Revenue from Contracts with Customers (ASU 2014-9) that requires companies to recognize revenue when a customer obtains control rather than when companies have transferred substantially all risks and rewards of a good or service. This update is effective for annual reporting periods beginning on or after December 15, 2017 and

interim periods therein and requires expanded disclosures. The Company is currently assessing the impact, if any, the adoption of ASU 2014-9 will have on its consolidated financial statements.

In July 2015, the Financial Accounting Standards Board issued Accounting Standards Update 2015-11, Simplifying the Measurement of Inventory (ASU 2015-11) which requires that inventory within the scope of this update, including inventory stated at average cost, be measured at the lower of cost and net realizable value. This update is effective for financial statements issued for fiscal years beginning after December 15, 2016, with early adoption permitted as of the beginning of an interim or annual reporting period. The adoption of this accounting guidance will not materially impact the Company's financial position.

In February 2016, the Financial Accounting Standards Board issued Accounting Standards Update 2016-2, Leases (ASU 2016-2) which requires lessees to recognize virtually all of their leases on the balance sheet, by recording a right-of-use asset and liability. This update is effective for financial statements issued for fiscal years beginning after December 15, 2018, with early adoption permitted as of the beginning of an interim or annual reporting period. The Company is currently assessing the impact the adoption of ASU 2016-2 will have on its consolidated financial statements.

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MERCER INTERNATIONAL INC.
NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**(Unaudited)****(In thousands of U.S. dollars, except share and per share data)****Note 1. The Company and Summary of Significant Accounting Policies (continued)**

In March 2016, the Financial Accounting Standards Board issued Accounting Standards Update 2016-9, Improvements to Employee Share-Based Payment Accounting (ASU 2016-9) which simplifies several aspects of accounting for share-based payment transactions including income tax consequences, classification of awards as either equity or liabilities, classification on the statement of cash flows and accounting for forfeitures. This update is effective for financial statements issued for fiscal years beginning after December 15, 2016. The Company is currently assessing the impact the adoption of ASU 2016-9 will have on its consolidated financial statements.

Note 2. Inventories

	March 31, 2016	December 31, 2015
Raw materials	\$ 52,494	\$ 57,592
Finished goods	29,821	36,829
Spare parts and other	51,373	46,580
	\$ 133,688	\$ 141,001

Note 3. Accounts Payable and Other

	March 31, 2016	December 31, 2015
Trade payables	\$ 25,550	\$ 20,637
Accrued expenses	54,892	55,648
Accrued interest payable	15,938	4,050
Interest rate derivative liability, current portion (Note 9)	10,951	10,380
Dividend payable (Note 6)	7,435	7,418
Other	7,278	5,317
	\$ 122,044	\$ 103,450

Note 4. Debt

	March 31, 2016	December 31, 2015
2019 Senior Notes, unsecured, \$227,000 face value (a)	\$ 223,336	\$ 245,689
2022 Senior Notes, unsecured, \$400,000 face value (a)	392,630	392,354
Revolving credit facilities		
75.0 million (b)	-	-
C\$40.0 million (c)	-	-
25.0 million (d)	-	-
5.0 million (e)	-	-
	\$ 615,966	\$ 638,043

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MERCER INTERNATIONAL INC.**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS****(Unaudited)****(In thousands of U.S. dollars, except share and per share data)****Note 4. Debt (continued)**

As at March 31, 2016, the maturities of the principal portion of debt are as follows:

2016	\$	-
2017		-
2018		-
2019		227,000
2020		-
Thereafter		400,000
	\$	627,000

Certain of the Company's debt instruments were issued under agreements which, among other things, may limit its ability and the ability of its subsidiaries to make certain payments, including dividends. These limitations are subject to specific exceptions. As at March 31, 2016, the Company is in compliance with the terms of its debt agreements.