SENSIENT TECHNOLOGIES CORP
Form 10-Q
May 08, 2009

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended: March 31, 2009

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: 1-7626

SENSIENT TECHNOLOGIES CORPORATION

(Exact name of registrant as specified in its charter)

Wisconsin	39-0561070
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

777 East Wisconsin Avenue, Milwaukee, Wisconsin 53202-5304

(Address of principal executive offices)

Registrant s telephone number, including area code: (414) 271-6755

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 at least 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 þ	Accelerated filer o	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

Indicate the number of shares outstanding of each of the issuer s classes of Common Stock, as of the latest practicable date.

Class	Outstanding at April 30, 2009
Common Stock, par value $0.10 per share	48,712,698

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SENSIENT TECHNOLOGIES CORPORATION
CONSOLIDATED CONDENSED STATEMENTS OF EARNINGS
(In thousands except per share amounts)
(Unaudited)

	Three Months Ended March 31, 2009	2008
Revenue	$ 282,824	$ 307,419
Cost of products sold	196,294	211,777
Selling and administrative expenses	48,146	56,009
Operating income	38,384	39,633
Interest expense	7,246	8,578
Earnings before income taxes	31,138	31,055
Income taxes	9,531	10,378
Net earnings	$ 21,607	$ 20,677
Average number of common shares outstanding:		
Basic	48,145	47,299
Diluted	48,351	47,806
Earnings per common share:		
Basic	$ .45	$ .44
Diluted	$ .45	$ .43
Dividends per common share	$ .19	$ .18

See accompanying notes to consolidated condensed financial statements.

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SENSIENT TECHNOLOGIES CORPORATION
CONSOLIDATED CONDENSED BALANCE SHEETS
(In thousands)

	March 31, 2009 (Unaudited)	December 31, 2008 *
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 8,358	$ 8,498
Trade accounts receivable, net	199,720	198,903
Inventories	369,073	381,246
Prepaid expenses and other current assets	39,461	38,876
TOTAL CURRENT ASSETS	616,612	627,523
OTHER ASSETS	39,261	40,878
INTANGIBLE ASSETS, NET	13,059	13,754
GOODWILL	426,780	440,416
PROPERTY, PLANT AND EQUIPMENT:		
Land	45,444	47,315
Buildings	242,335	248,366
Machinery and equipment	584,466	594,858
Construction in progress	43,620	40,200
	915,865	930,739
Less accumulated depreciation	(526,581)	(527,873)
	389,284	402,866
TOTAL ASSETS	$ 1,484,996	$ 1,525,437
LIABILITIES AND SHAREHOLDERS EQUITY		
CURRENT LIABILITIES:		
Trade accounts payable	$ 75,329	$ 82,976
Accrued salaries, wages and withholdings from employees	14,701	24,269
Other accrued expenses	49,002	52,825
Income taxes	4,692	1,988
Short-term borrowings	47,562	34,213
TOTAL CURRENT LIABILITIES	191,286	196,271
OTHER LIABILITIES	26,446	27,272
ACCRUED EMPLOYEE AND RETIREE BENEFITS	38,539	37,616
LONG-TERM DEBT	420,919	445,682
SHAREHOLDERS EQUITY:		
Common stock	5,396	5,396
Additional paid-in capital	83,130	82,261
Earnings reinvested in the business	885,830	873,444
Treasury stock, at cost	(113,402)	(116,217)

Accumulated other comprehensive loss	(53,148)	(26,288)
TOTAL SHAREHOLDERS EQUITY	807,806	818,596
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	$ 1,484,996	$ 1,525,437

See accompanying notes to consolidated condensed financial statements.

* Condensed from audited financial statements.

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SENSIENT TECHNOLOGIES CORPORATION
CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Three Months Ended March 31, 2009	Three Months Ended March 31, 2008
Net cash provided by operating activities	$ 17,536	$ 9,734
Cash flows from investing activities:		
Acquisition of property, plant and equipment	(8,836)	(12,113)
Proceeds from sale of assets	4	23
Other investing activity	(91)	1,462
Net cash used in investing activities	(8,923)	(10,628)
Cash flows from financing activities:		
Proceeds from additional borrowings	120,237	9,052
Debt payments	(122,234)	(3,071)
Dividends paid	(9,220)	(8,587)
Proceeds from options exercised and other equity transactions	2,261	5,478
Net cash (used in) provided by financing activities	(8,956)	2,872
Effect of exchange rate changes on cash and cash equivalents	203	308
Net (decrease) increase in cash and cash equivalents	(140)	2,286
Cash and cash equivalents at beginning of period	8,498	10,522
Cash and cash equivalents at end of period	$ 8,358	$ 12,808

See accompanying notes to consolidated condensed financial statements.

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SENSIENT TECHNOLOGIES CORPORATION
NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
(Unaudited)

1. Accounting Policies

In the opinion of Sensient Technologies Corporation (the Company), the accompanying unaudited consolidated condensed financial statements contain all adjustments (consisting of only normal recurring adjustments) which are necessary to present fairly the financial position of the Company as of March 31, 2009 and December 31, 2008, the results of operations for the three months ended March 31, 2009 and 2008, and cash flows for the three months ended March 31, 2009 and 2008. The results of operations for any interim period are not necessarily indicative of the results to be expected for the full year.

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Expenses are charged to operations in the year incurred. However, for interim reporting purposes, certain expenses are charged to operations based on a proportionate share of estimated annual amounts rather than as they are actually incurred.

Refer to the notes in the Company s annual consolidated financial statements for the year ended December 31, 2008, for additional details of the Company s financial condition and a description of the Company s accounting policies, which have been continued without change.

2. Share-Based Compensation

The Company adopted Statement of Financial Accounting Standards (SFAS) No. 123(R), *Share-Based Payment*, on January 1, 2006, using the modified prospective transition method. The Company recognized $0.8 million and $0.2 million of share-based compensation expense for the quarters ended March 31, 2009 and 2008, respectively.

The Company estimated the fair value of stock options using the Black-Scholes option pricing model. For the three months ended March 31, 2009 and 2008, the Company did not issue any stock options. The weighted-average fair value of stock options awarded during the year ended December 31, 2008 was $6.77 per share. Significant assumptions used in estimating the fair value of the awards granted during the year ended December 31, 2008 are as follows:

	2008
Dividend yield	2.3%
Volatility	26.3%
Risk-free interest rate	3.1%
Expected term (years)	5.3

3. Fair Value Measurements

On January 1, 2008 the Company adopted FASB Statement No. 157, *Fair Value Measurements.* This Statement defines fair value for financial assets and liabilities, establishes a framework for measuring fair value in generally accepted accounting principles (GAAP) and expands disclosures about fair value measurements. As of March 31, 2009 and 2008, the Company s only assets and liabilities subject to this statement are forward contracts (all currently accounted for as cash flow hedges) and mutual fund investments. Both of these financial instruments were previously being recorded by the Company at fair value that meets the requirements as defined by FASB

Statement No. 157. There was no impact on the Company s net earnings and financial position as a result of adopting this standard. The fair value of the forward contracts based on current pricing obtained for comparable derivative products (Level 2 inputs per Statement No. 157) at March 31, 2009 and 2008 was an asset of $0.5 million and $0.6 million, respectively. The fair value of the investments based on March 31, 2009 and 2008 market quotes (Level 1 inputs per Statement No. 157) was an asset of $13.1 million and $16.3 million, respectively.

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4. Segment Information

Operating results by segment for the periods and at the dates presented are as follows:

(In thousands)	Flavors & Fragrances	Color	Corporate & Other	Consolidated
Three months ended March 31, 2009:				
Revenue from external customers	$ 180,724	$ 83,677	$ 18,423	$ 282,824
Intersegment revenue	3,824	3,413	248	7,485
Total revenue	$ 184,548	$ 87,090	$ 18,671	$ 290,309
Operating income (loss)	$ 29,957	$ 13,731	$ (5,304)	$ 38,384
Interest expense			7,246	7,246
Earnings (loss) before income taxes	$ 29,957	$ 13,731	$ (12,550)	$ 31,138
Three months ended March 31, 2008:				
Revenue from external customers	$ 188,343	$ 98,501	$ 20,575	$ 307,419
Intersegment revenue	4,897	4,270	379	9,546
Total revenue	$ 193,240	$ 102,771	$ 20,954	$ 316,965
Operating income (loss)	$ 28,816	$ 18,505	$ (7,688)	$ 39,633
Interest expense			8,578	8,578
Earnings (loss) before income taxes	$ 28,816	$ 18,505	$ (16,266)	$ 31,055

Beginning in the first quarter of 2009, the Company s operations in Japan, previously reported in the Flavors & Fragrances Group, are reported in the Corporate and Other segment. Results for 2008 have been restated to reflect this change.

5. Inventories

At March 31, 2009 and December 31, 2008, inventories included finished and in-process products totaling $257.1 million and $269.8 million, respectively, and raw materials and supplies of $112.0 million and $111.4 million, respectively.

6. Retirement Plans

The Company s components of annual benefit cost for the defined benefit plans for the periods presented are as follows:

(In thousands)	Three Months Ended March 31, 2009	Three Months Ended March 31, 2008

Service cost	$ 340	$ 331
Interest cost	731	747
Expected return on plan assets	(263)	(287)
Amortization of prior service cost	456	487
Amortization of actuarial loss	50	58
Defined benefit expense	$ 1,314	$ 1,336

During the three months ended March 31, 2009, the Company made contributions to its defined benefit pension plans of $0.9 million. Total contributions to Company defined benefit pension plans are expected to be $4.3 million in 2009.

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7. Comprehensive Income

Comprehensive income is comprised of the following:

(In thousands)	Three Months Ended March 31, 2009	2008
Net earnings	$ 21,607	$ 20,677
Currency translation adjustments	(26,980)	27,179
Net gain on cash flow hedges	120	580
Net comprehensive (loss) income	$ (5,253)	$ 48,436

8. Cash Flows from Operating Activities

Cash flows from operating activities are detailed below:

(In thousands)	Three Months Ended March 31, 2009	2008
Cash flows from operating activities:		
Net earnings	$ 21,607	$ 20,677
Adjustments to arrive at net cash provided by operating activities:		
Depreciation and amortization	10,517	11,483
Stock-based compensation	781	180
Loss on assets	329	191
Deferred income taxes	959	1,041
Changes in operating assets and liabilities	(16,657)	(23,838)
Net cash provided by operating activities	$ 17,536	$ 9,734

9. Debt

In October 2008, the Company entered into a $105 million senior unsecured term loan agreement (Term Loan) with a group of five banks. As of March 31, 2009, the Company had borrowed the entire $105 million available and used the proceeds to repay amounts outstanding under the Company s committed revolving credit facility. On April 1, 2009, the Company borrowed under its revolving credit facility to retire the entire portion of the Company s public debt. The Term Loan matures on June 15, 2012 and the interest rate on the Term Loan is based on floating rates at the Company s election of either (1) the higher of (a) the prime rate or (b) the federal funds rate plus 0.5% or (2) a Eurodollar base rate derived from LIBOR plus a margin (initially 225 basis points but subject to adjustment as the Company s leverage ratio changes). The Company may prepay the Term Loan in whole or in part prior to the maturity date without any penalty.

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10. Derivative Instruments and Hedging Activity

On January 1, 2009, the Company adopted SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities*. This statement provides disclosure requirements pertaining to a Company s use of derivative instruments and its hedging activities. There is no impact on the Company s net earnings or financial position as a result of adopting this standard.

The Company may use derivative instruments for the purpose of hedging currency, commodity and interest rate exposures, which exist as part of ongoing business operations. As a policy, the Company does not engage in speculative or leveraged transactions, nor does the Company hold or issue financial instruments for trading purposes. Hedge effectiveness is determined by how closely the changes in the fair value of the hedging instrument offset the changes in the fair value or cash flows of the hedged transaction. Hedge accounting is permitted only if the hedging relationship is expected to be highly effective at the inception of the transaction and on an ongoing basis. Any ineffective portions are recognized in earnings immediately.

The Company manages its exposure to foreign exchange risk by the use of forward exchange contracts to reduce the effect of fluctuating foreign currencies on short-term foreign currency denominated intercompany transactions, non-functional currency raw material purchases and other known foreign currency exposures. These derivatives may or may not be designated as hedges under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities.* These forward exchange contracts have maturities of less than twelve months. The Company s primary hedging activities and their accounting treatment are summarized below:

Forward contracts designated as cash flow hedges The forward exchange contracts that have been designated as hedges, are accounted for as cash flow hedges. The Company had $106 million of forward exchange contracts, designated as hedges, outstanding as of March 31, 2009. The gains or losses on these instruments are deferred in accumulated other comprehensive income (OCI) until the underlying transaction is recognized in net earnings.

Forward contracts not designated as cash flow hedges The Company also utilizes forward exchange contracts that are not designated as cash flow hedges under SFAS No. 133. These contracts are marked-to-market in net earnings immediately, at the same time as the non-functional asset or liability is marked-to-market in net earnings. The Company had $34.3 million of forward exchange contracts, not designated as hedges, outstanding as of March 31, 2009 and recognized a loss of $0.3 million in net earnings for the three month period ended March 31, 2009.

Net Investment Hedges The Company has certain debt denominated in Euros and Swiss Francs. These debt instruments have been designated as partial hedges of the Company s Euro and Swiss Franc net asset positions. Changes in the fair value of this debt attributable to changes in the spot foreign exchange rate are recorded in foreign currency translation in OCI. As of March 31, 2009, the total value of the Company s Euro and Swiss Franc debt was $130.6 million. A gain of $7.5 million has been recorded as foreign currency translation in OCI for the three month period ended March 31, 2009.

The fair values of the Company s derivatives are recorded in the Company s consolidated balance sheet as follows:

	As of March 31, 2009			
(In thousands) Derivatives	Balance Sheet Location of Assets	Fair Value	Balance Sheet Location of Liabilities	Fair Value
Foreign exchange contracts designated as cash flow hedges	Other Assets	$ 767	Other Liabilities	$ 268
Foreign exchange contracts not designated as cash flow hedges	Other Assets	157	Other Liabilities	297
Total		$ 924		$ 565

The effect of the Company s cash flow hedges on the Company s Statement of Earnings is as follows:

	As of March 31, 2009		
(In thousands) Cash flow hedges	Amount of Gain in OCI	Gain reclassified into earnings (effective portion)	Gain (Loss) reclassified into earnings (ineffective portion)
Foreign exchange contracts	$106	$ 1,263	$

Over the next twelve months, the Company expects to reclassify $106,000 from OCI into net earnings.

11. Commitments and Contingencies

Environmental Matters

The Company is involved in various significant environmental matters, which are described below. The Company is also involved in other site closure and related environmental remediation and compliance activities at a manufacturing site related to a 2001 acquisition by the Company for which reserves for environmental matters were established as of the date of purchase. Actions that are legally required are substantially complete.

Superfund Claim

In July 2004, the Environmental Protection Agency (EPA) notified the Company s subsidiary Sensient Colors Inc. (Sensient Colors) that it may be a potentially responsible party (PRP) under the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) for activities at the General Color Company Superfund Site in Camden, New Jersey (the Site). The EPA requested reimbursement of $10.9 million in clean-up costs, plus interest. Sensient Colors advised the EPA that the Site had been expressly excluded from the Company s 1988 stock purchase of H. Kohnstamm & Company, Inc. (now Sensient Colors). The selling shareholders had retained ownership of and liability for the Site, and some became owners of

General Color Company, which continued to operate there until the mid-1990s. In a letter to the EPA in January 2005, the Company outlined legal challenges to the recoverability of certain costs and urged the EPA to pursue General Color Company and related parties. The EPA informed Sensient Colors that it was unwilling to discuss these legal challenges without prior conditions. In 2006, a private developer, Westfield Acres Urban Renewal Association II, LP, pursuant to an agreement with the EPA, began redevelopment efforts at the Site (construction of affordable housing) by demolishing buildings thereon. Thereafter, the EPA removed allegedly contaminated soil from the locations where the buildings once stood.

In March 2007, the United States filed a complaint in the U.S. District Court in New Jersey against Sensient Colors claiming over $16 million in response costs allegedly incurred and to be incurred by the EPA pursuant to CERCLA. Sensient Colors moved to dismiss the United States complaint, which motion was denied by the Court in October 2007. Sensient Colors timely filed its answer and affirmative defenses to the United States complaint, as well as a third-party complaint against current and former owners and/or operators of the Site. The United States moved to strike Sensient Colors affirmative defenses. In an August 12, 2008 Opinion and Order, following briefs and oral argument, the Court partly granted and partly denied the United States motion, effectively preserving most of Sensient Colors affirmative defenses, either as originally pled or with changes outlined by the Court. Sensient Colors promptly filed an amended pleading incorporating the revised affirmative defenses. On July 29, 2008, Sensient Colors filed a third-party complaint adding Kohnstamm Inc. (a Canadian affiliate of General Color Company) and its president Avtar Singh as defendants.

In late August 2008, in the course of reviewing docu