

PRICESMART INC
Form 10-Q
April 04, 2012

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 February 29, 2012

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 0-22793

PriceSmart, Inc.
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

33-0628530
(I.R.S. Employer
Identification No.)

9740 Scranton Road, San Diego, CA 92121
(Address of principal executive offices)

(858) 404-8800
(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 (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).

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Yes

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. (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 30,199,977 shares of its common stock, par value \$0.0001 per share, outstanding at March 31, 2012.

PRICESMART, INC.

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PART I—FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

PriceSmart, Inc.'s ("PriceSmart" or the "Company") unaudited consolidated balance sheet as of February 29, 2012 and the consolidated balance sheet as of August 31, 2011, the unaudited consolidated statements of income for the three and six months ended February 29, 2012 and February 28, 2011, the unaudited consolidated statements of equity for the six months ended February 29, 2012 and February 28, 2011, and the unaudited consolidated statements of cash flows for the six months ended February 29, 2012 and February 28, 2011, are included herein. Also included herein are the notes to the unaudited consolidated financial statements.

PRICESMART, INC.
CONSOLIDATED BALANCE SHEETS
(AMOUNTS IN THOUSANDS, EXCEPT SHARE DATA)

	February 29, 2012 (Unaudited)	August 31, 2011
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 90,799	\$ 76,817
Short-term restricted cash	1,288	1,240
Receivables, net of allowance for doubtful accounts of \$4 and \$5 as of February 29, 2012 and August 31, 2011, respectively	4,114	3,655
Merchandise inventories	179,904	177,232
Deferred tax assets – current	4,550	4,252
Prepaid expenses and other current assets	32,401	29,117
Assets of discontinued operations	46	464
Total current assets	313,102	292,777
Long-term restricted cash	36,662	22,626
Property and equipment, net	282,264	281,111
Goodwill	37,221	37,361
Deferred tax assets – long term	15,134	17,000
Other non-current assets	5,560	5,390
Investment in unconsolidated affiliates	7,584	8,063
Total Assets	\$ 697,527	\$ 664,328
LIABILITIES AND EQUITY		
Current Liabilities:		
Short-term borrowings	\$ 135	\$ 2,259
Accounts payable	167,418	163,432
Accrued salaries and benefits	11,052	11,681
Deferred membership income	13,185	11,416
Income taxes payable	7,754	7,655
Other accrued expenses	11,573	12,556
Dividends payable	9,063	—
Long-term debt, current portion	7,282	7,771
Deferred tax liability – current	364	533
Liabilities of discontinued operations	2	40
Total current liabilities	227,828	217,343
Deferred tax liability – long-term	1,615	1,888
Long-term portion of deferred rent	4,297	4,143
Long-term income taxes payable, net of current portion	3,380	3,310
Long-term debt, net of current portion	76,396	60,451
Other long-term liabilities (includes \$2.2 million and \$884,000 for the fair value of derivative instruments and \$561,000 and \$471,000 for the defined benefit plan as of February 29, 2012 and August 31, 2011, respectively)	2,760	1,355
Total liabilities	316,276	288,490

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Equity:

Common stock, \$0.0001 par value, 45,000,000 shares authorized; 30,840,358 and 30,695,933 shares issued and 30,199,395 and 29,900,030 shares outstanding (net of treasury shares) as of February 29, 2012 and August 31, 2011	3	3
Additional paid-in capital	381,037	383,549
Tax benefit from stock-based compensation	5,880	5,242
Accumulated other comprehensive loss	(33,828)	(22,915)
Retained earnings	44,324	28,238
Less: treasury stock at cost; 640,963 and 795,903 shares as of February 29, 2012 and August 31, 2011	(16,165)	(18,279)
Total equity	381,251	375,838
Total Liabilities and Equity	\$ 697,527	\$ 664,328

See accompanying notes.

PRICESMART, INC.
CONSOLIDATED STATEMENTS OF INCOME
(UNAUDITED—AMOUNTS IN THOUSANDS, EXCEPT PER SHARE DATA)

	Three Months Ended		Six Months Ended	
	February 29, 2012	February 28, 2011	February 29, 2012	February 28, 2011
Revenues:				
Net warehouse club sales	\$ 537,816	\$ 440,263	\$ 1,006,145	\$ 817,595
Export sales	3,459	1,872	5,708	3,280
Membership income	6,393	5,576	12,724	11,001
Other income	2,165	1,906	3,941	3,813
Total revenues	549,833	449,617	1,028,518	835,689
Operating expenses:				
Cost of goods sold:				
Net warehouse club	459,313	375,027	859,794	693,215
Export	3,292	1,758	5,453	3,102
Selling, general and administrative:				
Warehouse club operations	46,384	37,239	88,893	72,373
General and administrative	10,508	8,874	19,619	17,684
Pre-opening expenses	(1)	(15)	161	388
Total operating expenses	519,496	422,883	973,920	786,762
Operating income	30,337	26,734	54,598	48,927
Other income (expense):				
Interest income	205	239	389	367
Interest expense	(1,317)	(1,071)	(2,571)	(2,028)
Other income (expense), net	832	194	(437)	526
Total other expense	(280)	(638)	(2,619)	(1,135)
Income from continuing operations before provision for income taxes and loss of unconsolidated affiliates				
loss of unconsolidated affiliates	30,057	26,096	51,979	47,792
Provision for income taxes	(9,843)	(8,049)	(17,776)	(14,894)
Income (loss) of unconsolidated affiliates				
Income (loss) of unconsolidated affiliates	3	(37)	10	(42)
Income from continuing operations	20,217	18,010	34,213	32,856
Income (loss) from discontinued operations, net of tax				
Income (loss) from discontinued operations, net of tax	3	(93)	(4)	(86)
Net income	20,220	17,917	34,209	32,770
Net income per share available for distribution:				
Basic net income per share from continuing operations	\$ 0.67	\$ 0.60	\$ 1.14	\$ 1.11

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Basic net income (loss) per share from discontinued operations, net of tax	\$	—	\$	—	\$	—	\$	—
Basic net income per share	\$	0.67	\$	0.60	\$	1.14	\$	1.11
Diluted net income per share from continuing operations	\$	0.67	\$	0.60	\$	1.14	\$	1.11
Diluted net income (loss) per share from discontinued operations, net of tax	\$	—	\$	—	\$	—	\$	—
Diluted net income per share	\$	0.67	\$	0.60	\$	1.14	\$	1.11
Shares used in per share computations:								
Basic		29,541		29,414		29,522		29,385
Diluted		29,553		29,423		29,535		29,392
Dividends per share	\$	0.60	\$	0.60	\$	0.60	\$	0.60

See accompanying notes.

PRICESMART, INC.
CONSOLIDATED STATEMENTS OF EQUITY
(UNAUDITED—AMOUNTS IN THOUSANDS)

	Common Shares	Stock Amount	Additional Paid-in Capital	Tax Benefit From Stock- based Compen- sation	Accum- ulated Other Compre- hensive Loss	Retained Earnings (Accum- ulated Deficit)	Treasury Stock Shares	Treasury Stock Amount	Total Equity
Balance at August 31, 2010	30,625	\$ 3	\$ 379,368	\$ 4,490	\$ (16,672)	\$ (15,578)	727	\$ (15,568)	\$ 336,043
Purchase of treasury stock	—	—	—	—	—	—	65	(2,513)	(2,513)
Issuance of restricted stock awards	62	—	—	—	—	—	—	—	—
Forfeiture of restricted stock awards	(2)	—	—	—	—	—	—	—	—
Exercise of stock options	4	—	104	—	—	—	—	—	104
Stock-based compensation	—	—	1,964	881	—	—	—	—	2,845
Dividend payable to stockholders	—	—	—	—	—	(8,969)	—	—	(8,969)
Dividend paid to stockholders	—	—	—	—	—	(8,969)	—	—	(8,969)
Change in fair value of interest rate swaps	—	—	—	—	137	—	—	—	137
Net income	—	—	—	—	—	32,770	—	—	32,770
Translation adjustment	—	—	—	—	(30)	—	—	—	(30)
Comprehensive income									32,877
Balance at February 28, 2011	30,689	\$ 3	\$ 381,436	\$ 5,371	\$ (16,565)	\$ (746)	792	\$ (18,081)	\$ 351,418
Balance at August 31, 2011	30,696	\$ 3	\$ 383,549	\$ 5,242	\$ (22,915)	\$ 28,238	796	\$ (18,279)	\$ 375,838
Purchase of treasury stock	—	—	—	—	—	—	42	(2,839)	(2,839)

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Issuance of treasury stock	(197)	—	(4,953)			(197)	4,953		
Issuance of restricted stock awards	337	—	—	—	—	—	—	—	—
Forfeiture of restricted stock awards	(2)	—	—	—	—	—	—	—	—
Exercise of stock options	6	—	89	—	—	—	—	—	89
Stock-based compensation	—	—	2,352	638	—	—	—	—	2,990
Dividend payable to stockholders	—	—	—	—	—	(9,063)	—	—	(9,063)
Dividend paid to stockholders	—	—	—	—	—	(9,060)	—	—	(9,060)
Change in fair value of interest rate swaps, net of tax	—	—	—	—	(1,355)	—	—	—	(1,355)
Amortization of prior service costs on defined benefit plan, net of tax	—	—	—	—	12	—	—	—	12
Net income	—	—	—	—	—	34,209	—	—	34,209
Translation adjustment to record merger of subsidiaries and correction to translation of Property and Equipment, net	—	—	—	—	(8,881)	—	—	—	(8,881)
Translation adjustment	—	—	—	—	(689)	—	—	—	(689)
Comprehensive income	—	—	—	—	—	—	—	—	23,296
Balance at February 29, 2012	30,840	\$ 3	\$ 381,037	\$ 5,880	\$ (33,828)	\$ 44,324	641	\$ (16,165)	\$ 381,251

See accompanying notes.

PRICESMART, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED—AMOUNTS IN THOUSANDS)

	Six Months Ended	
	February 29, 2012	February 28, 2011
Operating Activities:		
Net income	\$ 34,209	\$ 32,770
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	11,550	8,836
Allowance for doubtful accounts	(1)	1
(Gain) loss on sale of property and equipment	152	353
Deferred income taxes	1,764	2,316
Discontinued operations	4	(86)
Excess tax deficiency (benefit) on stock-based compensation	(638)	(881)
Equity in gains/(losses) of unconsolidated affiliates	(10)	42
Stock-based compensation	2,352	1,964
Change in operating assets and liabilities:		
Change in receivables, prepaid expenses and other current assets, accrued salaries and benefits, deferred membership income and other accruals	(3,455)	(5,391)
Merchandise inventories	(2,674)	(20,502)
Accounts payable	3,987	18,166
Net cash provided by (used in) continuing operating activities	47,240	37,588
Net cash provided by (used in) discontinued operating activities	375	77
Net cash provided by (used in) operating activities	47,615	37,665
Investing Activities:		
Additions to property and equipment	(21,762)	(21,635)
Proceeds from disposal of property and equipment	37	142
Net cash flows provided by (used in) investing activities	(21,725)	(21,493)
Financing Activities:		
Proceeds from bank borrowings	71,698	25,464
Repayment of bank borrowings	(59,277)	(25,095)
Release of (addition to) restricted cash	(14,000)	(8,000)
Cash dividend payments	(9,060)	(8,969)
Excess tax (deficiency) benefit on stock-based compensation	638	881
Purchase of treasury stock	(2,839)	(2,513)
Proceeds from exercise of stock options	89	104
Net cash provided by (used in) financing activities	(12,751)	(18,128)
Effect of exchange rate changes on cash and cash equivalents	843	(731)
Net increase (decrease) in cash and cash equivalents	13,982	(2,687)
Cash and cash equivalents at beginning of period	76,817	73,346
Cash and cash equivalents at end of period	\$ 90,799	\$ 70,659
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		

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Interest, net of amounts capitalized	\$	2,347	\$	1,893
Income taxes	\$	15,297	\$	11,504
Supplemental non-cash item:				
Cancellation of joint ventures Prico Enterprise loan	\$	(473)	\$	—
Dividends declared but not paid	\$	9,063	\$	8,969

PRICESMART, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

February 29, 2012

NOTE 1 – COMPANY OVERVIEW AND BASIS OF PRESENTATION

PriceSmart, Inc.'s ("PriceSmart" or the "Company") business consists primarily of international membership shopping warehouse clubs similar to, but smaller in size than, warehouse clubs in the United States. As of February 29, 2012, the Company had 29 consolidated warehouse clubs in operation in 12 countries and one U.S. territory (five in Costa Rica, four each in Panama and Trinidad, three each in Guatemala and in the Dominican Republic, two each in El Salvador and Honduras and one each in Colombia, Aruba, Barbados, Jamaica, Nicaragua and the United States Virgin Islands), of which the Company owns 100% of the corresponding legal entities (see Note 2 - Summary of Significant Accounting Policies). The Company opened a new warehouse club in Santo Domingo, Dominican Republic ("Arroyo Hondo") on November 5, 2010 and a new membership warehouse club in Barranquilla, Colombia on August 19, 2011. The Company also acquired land in south Cali, Colombia, on December 14, 2011 upon which it currently anticipates opening a new warehouse club in October 2012. Additionally, on January 9, 2012 the Company entered into an agreement to acquire property located in La Union, Cartago, Costa Rica, upon which the Company anticipates constructing its sixth membership warehouse club in Costa Rica with an anticipated opening in the summer of calendar year 2013. Finally, on March 15, 2012 the Company acquired land in north Cali, Colombia upon which it anticipates opening a new warehouse club in the spring of calendar year 2013. The initial warehouse sales and membership results experienced with the opening of the Barranquilla warehouse club has reinforced the Company's belief that Colombia could be a market for multiple PriceSmart warehouse clubs. The Company continues to explore other potential sites for future warehouse clubs in other major cities in Colombia as well as in its other markets.

Basis of Presentation - The interim consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q for interim financial reporting pursuant to the rules and regulations of the U.S. Securities and Exchange Commission ("SEC"). These interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the Company's Amendment No. 1 to Annual Report on Form 10-K/A for the fiscal year ended August 31, 2011 (the "2011 Form 10-K"). The interim consolidated financial statements include the accounts of PriceSmart, Inc., a Delaware corporation, and its subsidiaries. Intercompany transactions between the Company and its subsidiaries have been eliminated in consolidation.

In accordance with the Financial Accounting Standards Board's ("FASB") revised guidance establishing general accounting standards and disclosure of subsequent events, the Company has evaluated subsequent events through the date and time these financial statements were issued.

During fiscal year 2007 and during the first quarter of fiscal year 2012, the Company merged in each period a wholly owned subsidiary formed to purchase, develop and serve as a holding company for the land and buildings used by certain operating warehouse clubs (each, a "Landco") with one of the wholly owned subsidiaries formed to operate these warehouse clubs (each, an "Opco"). Each of the Landcos involved in these mergers had a functional and reporting currency in U.S. dollars, and each of the related Opcos that they were merged into had a foreign currency as a functional currency and U.S. dollars as a reporting currency. In each of these mergers, the Opco was the surviving entity, with the assets, liabilities and equity accounts of the Landco being transferred to the Opco and the Landco subsidiary ceasing to exist. Since the Landco entity ceased to exist, and all relevant economic activities previously performed by the Landco no longer exist, a significant change in economic facts and circumstances has been

determined to have taken place, indicating that the functional currency has changed as the assets were transferred to the Opco. Upon this transfer, the Company is required to remeasure the nonmonetary balance sheet items at historical exchange rates in order to produce the same result in terms of the functional currency that would have occurred if those items had been initially recorded in the foreign functional currency. As a result of the 2012 merger, and the resulting translation adjustments, the Company recorded in the first quarter of fiscal year 2012 a charge to comprehensive income for approximately \$5.6 million relating to the fiscal year 2012 merger, with a corresponding reduction to Property and equipment, net for the same amount.

During the first quarter of fiscal year 2012, the Company identified errors in the consolidated financial statements for the fiscal year ended August 31, 2011 and for fiscal years previous to 2009. The errors relate to incorrect (i) accounting for the 2007 merger described above which impacted the translation of Property and equipment, net from foreign currencies to U.S. dollars and the related offset to Accumulated other comprehensive loss; and (ii) the translation of Property and equipment, net from foreign currencies to U.S. dollars and the related offset to Accumulated other comprehensive loss. The correction of these errors would have decreased comprehensive income by \$6.4 million and increased comprehensive income by \$3.1 million in fiscal year 2007 and 2011, respectively. The total of these corrections, which was recorded in the first quarter of fiscal 2012 as a charge to comprehensive income was approximately \$3.3 million and decreased Property and equipment, net and increased Accumulated other comprehensive loss by the same amount.

The Company has analyzed the impact of these items and concluded that neither error would be material to any individual period, taking into account the requirements of the Securities and Exchange Commission ("SEC") Staff Accounting Bulletin No. 108, Considering the Effects of Prior Year Misstatements in the Current Year Financial Statements ("SAB 108"). In accordance with the relevant guidance, management evaluated the materiality of errors from a quantitative and qualitative perspective. Based on such evaluation, the Company concluded that correcting the cumulative errors, which decreased comprehensive income by approximately \$3.3 million for the three month period ended November 30, 2011, would be immaterial to the expected full year results for fiscal 2012 and financial position as presented on the consolidated balance sheet. Correcting the error would not have had a material impact on any individual prior period presented in the 2011 Form 10-K or affect the trend of financial results. As provided by SAB 108, the error correction did not require the restatement of the consolidated financial statements for prior periods.

PRICESMART, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

As a result of recording (i) the fiscal year 2012 merger and the resulting translation adjustment, (ii) the correction of the accounting for the 2007 merger, and (iii) the correction of an error in translation of Property and equipment, net from foreign currencies to U.S. dollars, the Company recorded an increase to Accumulated other comprehensive loss for \$8.9 million within the first quarter of fiscal year 2012.

Monetary assets and liabilities in currencies other than the functional currency of the respective entity are revalued to the functional currency using the exchange rate on the balance sheet date. These foreign exchange transaction gains (losses), including repatriation of funds, have been reclassified from Cost of goods sold to Other income (expense) in the Consolidated Statements of Income for the fiscal year and interim periods reported for 2011. The Company's management believes that these foreign currency transactions are not directly matched to the recognition of cost of goods sold but are more closely linked to financing activities of the Company. These activities include the use of the extension of U.S dollar payables as a funding tool to meet the Company's subsidiary cash requirements and direct bank financing for U.S. dollar loans that constitute financing vehicles for expansion or development of subsidiaries, where once the cash is deposited into that subsidiary, it is fungible and can be used for any cash requirement of the entity such as capital, intercompany payments, working capital requirements, dividend payments and increases in restricted cash balances to comply with financing requirements. The Company believes that these reclassifications will allow for better comparability to other comparable companies with similar business models. The following table summarizes the amounts reclassified to conform with fiscal year 2012 presentation (in thousands):

	Three Months Ended				Total fiscal year 2011
	November 30, 2010	February 28, 2011	May 31, 2011	August 31, 2011	
Other income (expense) – (net previously reported)(1)	\$ (46)	\$ (260)	\$ 1,838	\$ 8	\$ 1,540
Foreign exchange transaction gains reclassified from Cost of goods sold to Other income (expenses), net	378	454	529	963	2,324
Other income (expense), net – (currently reported)(2)	\$ 332	\$ 194	\$ 2,367	\$ 971	\$ 3,864

	Three Months Ended				Total fiscal year 2011
	November 30, 2010	February 28, 2011	May 31, 2011	August 31, 2011	
Composition of beginning balance Other income (expense) – (1)(previously reported):					
Gain/(loss) on sale	(53)	(176)	1,179	(187)	763
Currency gain/(loss)	7	(84)	659	195	777

Composition of ending
balance Other income
(expense) – (as now
(2)reported):