WESCO INTERNATIONAL INC
Form 10-Q
October 30, 2015
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 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 September 30, 2015
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: 001-14989
WESCO International, Inc.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	25-1723342 (I.R.S. Employer Identification No.)
225 West Station Square Drive Suite 700 Pittsburgh, Pennsylvania (Address of principal executive offices)	15219 (Zip Code)

(412) 454-2200
(Registrant's telephone number, including area code)
Not applicable.
(Former name, former address and former fiscal year, if changed since last report)

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 þ 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.

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

As of October 29, 2015, 42,131,220 shares of common stock, $.01 par value, of the registrant were outstanding.

WESCO INTERNATIONAL, INC. AND SUBSIDIARIES

QUARTERLY REPORT ON FORM 10-Q

Table of Contents

WESCO INTERNATIONAL, INC. AND SUBSIDIARIES

PART I—FINANCIAL INFORMATION

Item 1. Financial Statements.

The interim financial information required by this item is set forth in the Condensed Consolidated Financial Statements and Notes thereto in this Quarterly Report on Form 10-Q, as follows:

WESCO INTERNATIONAL, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands of dollars, except share data)
(unaudited)

	September 30, 2015	December 31, 2014
Assets		
Current assets:		
Cash and cash equivalents	$132,852	$128,319
Trade accounts receivable, net of allowance for doubtful accounts of $22,513 and $21,084 in 2015 and 2014, respectively	1,149,743	1,117,420
Other accounts receivable	71,253	138,745
Inventories, net	844,955	819,502
Prepaid expenses and other current assets	167,287	146,352
Total current assets	2,366,090	2,350,338
Property, buildings and equipment, net of accumulated depreciation of $239,604 and $229,196 in 2015 and 2014, respectively	171,789	182,725
Intangible assets, net of accumulated amortization of $130,929 and $110,828 in 2015 and 2014, respectively	388,988	429,840
Goodwill	1,666,218	1,735,440
Other assets	49,424	56,094
Total assets	$4,642,509	$4,754,437
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$787,637	$765,135
Accrued payroll and benefit costs	45,736	67,935
Short-term debt	44,419	46,787
Current portion of long-term debt	2,144	2,343
Other current liabilities	136,841	181,672
Total current liabilities	1,016,777	1,063,872
Long-term debt, net of discount of $165,714 and $170,367 in 2015 and 2014, respectively	1,454,705	1,366,430
Deferred income taxes	361,678	346,743
Other noncurrent liabilities	49,501	49,227
Total liabilities	$2,882,661	$2,826,272
Commitments and contingencies (Note 8)		
Stockholders' equity:		
Preferred stock, $.01 par value; 20,000,000 shares authorized, no shares issued or outstanding	—	—
Common stock, $.01 par value; 210,000,000 shares authorized, 58,587,349 and 58,400,736 shares issued and 42,164,170 and 44,489,989 shares outstanding in 2015 and 2014, respectively	586	584
Class B nonvoting convertible common stock, $.01 par value; 20,000,000 shares authorized, 4,339,431 issued and no shares outstanding in 2015 and 2014, respectively	43	43
Additional capital	1,114,299	1,102,369
Retained earnings	1,806,052	1,643,914
	(772,659)	(616,366)

Treasury stock, at cost; 20,762,610 and 18,250,178 shares in 2015 and 2014, respectively		
Accumulated other comprehensive loss	(385,526)	(201,892)
Total WESCO International, Inc. stockholders' equity	1,762,795	1,928,652
Noncontrolling interests	(2,947)	(487)
Total stockholders’ equity	1,759,848	1,928,165
Total liabilities and stockholders’ equity	$4,642,509	$4,754,437

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

WESCO INTERNATIONAL, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME (LOSS)
(In thousands of dollars, except per share data)
(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Net sales	$1,923,899	$2,078,150	$5,656,947	$5,894,141
Cost of goods sold (excluding depreciation and amortization below)	1,543,113	1,655,787	4,526,836	4,685,257
Selling, general and administrative expenses	258,151	271,697	797,980	815,869
Depreciation and amortization	16,287	17,418	48,347	50,976
Income from operations	106,348	133,248	283,784	342,039
Interest expense, net	20,417	20,798	59,924	61,823
Income before income taxes	85,931	112,450	223,860	280,216
Provision for income taxes	23,547	31,632	64,047	78,757
Net income	62,384	80,818	159,813	201,459
Net (loss) income attributable to noncontrolling interests	(1,119)	2	(2,460)	(64)
Net income attributable to WESCO International, Inc.	$63,503	$80,816	$162,273	$201,523
Other comprehensive loss:				
Foreign currency translation adjustments	(95,377)	(63,794)	(183,634)	(67,271)
Comprehensive (loss) income attributable to WESCO International, Inc.	$(31,874)	$17,022	$(21,361)	$134,252
Earnings per share attributable to WESCO International, Inc.				
Basic	$1.47	$1.82	$3.70	$4.54
Diluted	$1.28	$1.52	$3.16	$3.78

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

WESCO INTERNATIONAL, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands of dollars)
(unaudited)

	Nine Months Ended September 30, 2015	2014
Operating activities:		
Net income	$159,813	$201,459
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	48,347	50,976
Deferred income taxes	26,339	17,847
Other operating activities, net	17,498	4,744
Changes in assets and liabilities:		
Trade accounts receivable, net	(49,799)	(174,438)
Other accounts receivable	64,893	(2,779)
Inventories, net	(38,862)	(54,053)
Prepaid expenses and other assets	(12,052)	(35,097)
Accounts payable	30,389	106,886
Accrued payroll and benefit costs	(20,394)	7,748
Other current and noncurrent liabilities	(50,208)	16,527
Net cash provided by operating activities	175,964	139,820
Investing activities:		
Acquisition payments, net of cash acquired	(68,502)	(138,805)
Capital expenditures	(16,242)	(16,036)
Other investing activities	1,791	5,444
Net cash used in investing activities	(82,953)	(149,397)
Financing activities:		
Proceeds from issuance of short-term debt	75,564	49,727
Repayments of short-term debt	(73,464)	(42,168)
Proceeds from issuance of long-term debt	1,220,334	912,146
Repayments of long-term debt	(1,128,694)	(885,408)
Repayment of deferred acquisition payable	—	(29,395)
Repurchases of common stock (Note 5)	(155,775)	(6,931)
Other financing activities, net	(11,253)	(2,381)
Net cash used in financing activities	(73,288)	(4,410)
Effect of exchange rate changes on cash and cash equivalents	(15,190)	630
Net change in cash and cash equivalents	4,533	(13,357)
Cash and cash equivalents at the beginning of period	128,319	123,725
Cash and cash equivalents at the end of period	$132,852	$110,368

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

5

WESCO INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. ORGANIZATION

WESCO International, Inc. and its subsidiaries (collectively, “WESCO” or the "Company"), headquartered in Pittsburgh, Pennsylvania, is a full-line distributor of electrical, industrial and communications maintenance, repair and operating (“MRO”) and original equipment manufacturers (“OEM”) products, construction materials, and advanced supply chain management and logistics services used primarily in the industrial, construction, utility and commercial, institutional and government markets. WESCO serves over 75,000 active customers globally, through approximately 485 full service branches and nine distribution centers located primarily in the United States, Canada and Mexico, with operations in 16 additional countries.

2. ACCOUNTING POLICIES

Basis of Presentation

The accompanying unaudited Condensed Consolidated Financial Statements of WESCO have been prepared in accordance with Rule 10-01 of Regulation S-X of the Securities and Exchange Commission (the “SEC”). The unaudited condensed consolidated financial information should be read in conjunction with the audited Consolidated Financial Statements and Notes thereto included in WESCO’s 2014 Annual Report on Form 10-K as filed with the SEC on February 24, 2015. The Condensed Consolidated Balance Sheet at December 31, 2014 was derived from the audited Consolidated Financial Statements as of that date, but does not include all of the disclosures required by accounting principles generally accepted in the United States of America.

The unaudited Condensed Consolidated Balance Sheet as of September 30, 2015, the unaudited Condensed Consolidated Statements of Income and Comprehensive Income (Loss) for the three and nine months ended September 30, 2015 and 2014, respectively, and the unaudited Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2015 and 2014, respectively, in the opinion of management, have been prepared on the same basis as the audited Consolidated Financial Statements and include all adjustments necessary for the fair statement of the results of the interim periods presented herein. All adjustments reflected in the unaudited condensed consolidated financial information are of a normal recurring nature unless indicated. The results for the interim periods presented herein are not necessarily indicative of the results to be expected for the full year.

The Condensed Consolidated Balance Sheet at December 31, 2014 and the unaudited Condensed Consolidated Statement of Cash Flows for the nine months ended September 30, 2014 include certain reclassifications to previously reported amounts to conform to the current period presentation.

Fair Value of Financial Instruments

The Company measures the fair value of financial assets and liabilities in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 820, "Fair Value Measurements and Disclosures," which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements.

ASC 820 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value and requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that are accessible at the measurement date.
- Level 2 inputs include inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices in active markets for similar assets and liabilities, quoted prices for identical or similar assets or liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of assets or liabilities.

- Level 3 inputs are unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions.

At September 30, 2015, the carrying value of WESCO’s 6.0% Convertible Senior Debentures due 2029 (the "2029 Debentures") was $180.5 million and the fair value was approximately $578.4 million. At December 31, 2014, the carrying value of WESCO’s 2029 Debentures was $177.6 million and the fair value was approximately $936.1 million. The reported

6

carrying amounts of WESCO’s other debt instruments approximate their fair values. The Company uses a market approach to fair value all of its debt instruments, utilizing quoted prices in active markets, interest rates and other relevant information generated by market transactions involving similar instruments. Therefore, all of the Company's debt instruments are classified as Level 2 within the valuation hierarchy. For all of the Company's remaining financial instruments, consisting of cash and cash equivalents, accounts receivable, accounts payable and other accrued liabilities, carrying values are considered to approximate fair value due to the short maturity of these instruments.

New Accounting Pronouncements

In June 2014, the FASB issued Accounting Standards Update ("ASU") 2014-12, Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period. The amendments in this ASU require a reporting entity to treat a performance target that affects vesting and could be achieved after the requisite service period as a performance condition. A reporting entity should apply FASB ASC Topic 718, Compensation—Stock Compensation, to awards with performance conditions that affect vesting. For all entities, ASU 2014-12 is effective for annual periods and interim periods within those annual periods, beginning after December 15, 2015. Early adoption is permitted. This ASU may be adopted either prospectively for share-based payment awards granted or modified on or after the effective date, or retrospectively, using a modified retrospective approach. The modified retrospective approach would apply to share-based payment awards outstanding as of the beginning of the earliest annual period presented in the financial statements on adoption and to all new or modified awards thereafter. The adoption of this guidance is not expected to have a material impact on WESCO's financial position, results of operations or cash flows.

In August 2015, the FASB issued ASU 2015-14, Revenue from Contracts with Customers: Deferral of Effective Date. The Company previously reported that in May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers, which provides a framework for addressing revenue recognition issues and replaces almost all existing revenue recognition guidance in current U.S. generally accepted accounting principles. The core principle of ASU 2014-09 is for companies to recognize revenue for the transfer of goods or services to customers in amounts that reflect the consideration to which the company expects to be entitled in exchange for those goods or services. ASU 2014-09 will also result in enhanced disclosures about revenue, provide guidance for transactions that were not previously addressed comprehensively, and improve guidance for multiple-element arrangements. The amendments in ASU 2015-14 defer the effective date of the new revenue recognition guidance to annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early adoption is permitted to the original effective date of December 15, 2016, including interim periods within that reporting period. Management is currently evaluating the future impact of this guidance on WESCO's consolidated financial statements and notes thereto.

In August 2015, the FASB issued ASU 2015-15, Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements. The Company previously reported that in April 2015, the FASB issued ASU 2015-03, Simplifying the Presentation of Debt Issuance Costs, which simplifies the presentation of debt issuance costs by requiring that debt issuance costs related to a recognized liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The amendments in ASU 2015-15 address the absence of authoritative guidance within ASU 2015-03 for debt issuance costs related to line-of-credit arrangements such that the SEC staff would not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the line-of-credit arrangement. ASU 2015-15 and ASU 2015-03 are effective for financial statements of public business entities issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. Early adoption is permitted for financial statements that have not been previously issued. The adoption of this guidance is not expected to have a material impact on WESCO's financial position, results of operations or cash flows.

In September 2015, the FASB issued ASU 2015-16, Business Combinations: Simplifying the Accounting for Measurement-Period Adjustments. The amendments in this ASU require that an acquirer recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined; calculated as if the accounting had been completed at the acquisition date. For public business entities, the amendments in this ASU are effective for fiscal years beginning after December 15, 2015, including interim periods within those fiscal years. The amendments in this ASU should be applied prospectively with earlier application permitted for financial statements that have not been issued. The adoption of this guidance is not expected to have a material impact on WESCO's financial position, results of operations or cash flows.
Management does not believe that any other recently issued, but not yet effective, accounting standards if currently adopted would have a material effect on the accompanying financial statements and notes thereto.

WESCO INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(CONTINUED)
(unaudited)

3. ACQUISITIONS

The following table sets forth the consideration paid for acquisitions:

	Nine Months Ended	
(In thousands of dollars)	September 30, 2015	September 30, 2014
Fair value of assets acquired	$89,786	$153,430
Fair value of liabilities assumed	21,284	14,625
Cash paid for acquisitions, net of cash acquired	$68,502	$138,805

The fair values of assets acquired and liabilities assumed during the nine months ended September 30, 2015, which are primarily for the acquisition of Hill Country Electric Supply, LP ("Hill Country"), are based upon preliminary calculations and valuations. WESCO's estimates and assumptions for its preliminary purchase price allocation are subject to change as it obtains additional information for its estimates during the respective measurement periods (up to one year from the respective acquisition date).

2015 Acquisition of Hill Country Electric Supply, LP

On May 1, 2015, WESCO Distribution, Inc. completed the acquisition of Hill Country, an electrical distributor focused on the commercial construction market from nine locations in Central and South Texas with approximately $140 million in annual sales. WESCO funded the purchase price paid at closing with borrowings under its prior revolving credit facility. The purchase price was allocated to the respective assets and liabilities based upon their estimated fair values as of the acquisition date. The preliminary fair value of intangibles was estimated by management and the allocation resulted in intangible assets of $21.1 million and goodwill of $15.8 million. The intangible assets include customer relationships of $13.1 million amortized over 11 years, non-compete agreements of $0.2 million amortized over 5 years, and trademarks of $7.8 million amortized over 12 years. No residual value is estimated for the intangible assets being amortized. Management believes that the majority of goodwill is deductible for tax purposes.

2014 Acquisitions of LaPrairie, Inc., Hazmasters, Inc. and Hi-Line Utility Supply.

On February 1, 2014, WESCO Distribution, Inc., through its wholly-owned Canadian subsidiary, completed the acquisition of LaPrairie, Inc. ("LaPrairie"), a wholesale distributor of electrical products with approximately $30 million in annual sales servicing the transmission, distribution, and substation needs of utilities and utility contractors from a single location in Newmarket, Ontario. WESCO funded the purchase price paid at closing with cash. The purchase price was allocated to the respective assets and liabilities based upon their estimated fair values as of the acquisition date. The fair value of intangibles was estimated by management and the allocation resulted in intangible assets of $11.0 million and goodwill of $8.9 million. The majority of goodwill is deductible for tax purposes.

On March 17, 2014, WESCO Distribution, Inc., through its wholly-owned Canadian subsidiary, completed the acquisition of Hazmasters, Inc. ("Hazmasters"), a leading independent Canadian distributor of safety products with approximately $80 million in annual sales servicing customers in the industrial, construction, commercial, institution, and government markets from 14 branches across Canada. WESCO funded the purchase price paid at closing with cash and borrowings under its prior revolving credit facility. The purchase price was allocated to the respective assets and liabilities based upon their estimated fair values as of the acquisition date. The fair value of intangibles was estimated by management and the allocation resulted in intangible assets of $28.1 million and goodwill of $29.5 million, which is not deductible for tax purposes.

On June 11, 2014, WESCO Distribution, Inc., completed the acquisition of Hi-Line Utility Supply ("Hi-Line"), a provider of utility MRO and safety products, as well as rubber goods testing and certification services, with approximately $30 million in annual sales from locations in Chicago, Illinois and Millbury, Massachusetts. WESCO funded the purchase price paid at closing with cash. The purchase price was allocated to the respective assets and liabilities based upon their estimated fair values as of the acquisition date. The fair value of intangibles was estimated by management and the allocation resulted in intangible assets of $14.2 million and goodwill of $24.0 million. The majority of goodwill is deductible for tax purposes.

For all acquisitions made in the first nine months of 2014, the intangible assets include customer relationships of $38.9 million amortized over 2 to 12 years, supplier relationships of $3.2 million amortized over 10 years, trademarks of $10.9 million, and other intangibles of $0.3 million. Certain trademarks have been assigned an indefinite life while others are amortized over 5 and 10 years. No residual value is estimated for the intangible assets being amortized.

WESCO INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(CONTINUED)
(unaudited)

4. STOCK-BASED COMPENSATION

WESCO's stock-based employee compensation plans are comprised of stock-settled stock appreciation rights, restricted stock units and performance-based awards. Compensation cost for all stock-based awards is measured at fair value on the date of grant and compensation cost is recognized, net of estimated forfeitures, over the service period for awards expected to vest. The fair value of stock-settled stock appreciation rights and performance-based awards with market conditions is determined using the Black-Scholes and Monte Carlo simulation models, respectively. The fair value of restricted stock units and performance-based awards with performance conditions is determined by the grant-date closing price of WESCO's common stock. The forfeiture assumption is based on WESCO's historical employee behavior that is reviewed on an annual basis. No dividends are assumed.

During the three and nine months ended September 30, 2015 and 2014, WESCO granted the following stock-settled appreciation rights, restricted stock units and performance-based awards at the following weighted-average fair values:

	Three Months Ended		Nine Months Ended	
	September 30, 2015	September 30, 2014	September 30, 2015	September 30, 2014
Stock-settled appreciation rights granted	—	—	394,182	274,508
Weighted-average fair value	$—	$—	$21.68	