GREENBRIER COMPANIES INC
Form 10-Q
January 09, 2007

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

Form 10-Q

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

for the quarterly period ended November 30, 2006

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 No. 1-13146

THE GREENBRIER COMPANIES, INC.
(Exact name of registrant as specified in its charter)

Oregon (State of Incorporation)	93-0816972 (I.R.S. Employer Identification No.)
One Centerpointe Drive, Suite 200, Lake Oswego, OR (Address of principal executive offices)	97035 (Zip Code)

(503) 684-7000
(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 þ No o

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 o Accelerated filer þ Non-accelerated filer 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

The number of shares of the registrant s common stock, without par value, outstanding on January 3, 2007 was 15,971,155 shares.

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THE GREENBRIER COMPANIES, INC.

PART I. FINANCIAL INFORMATION

Item 1. Condensed Financial Statements

Consolidated Balance Sheets

(In thousands, except per share amounts, unaudited)

	November 30, 2006	August 31, 2006
Assets		
Cash and cash equivalents	$ 14,359	$ 142,894
Restricted cash	2,603	2,056
Accounts and notes receivable	145,392	115,565
Inventories	209,277	163,151
Assets held for sale	67,750	35,216
Equipment on operating leases	303,280	301,009
Investment in direct finance leases	8,456	6,511
Property, plant and equipment	115,221	80,034
Goodwill and intangibles	188,063	3,340
Other	28,197	27,538
	$ 1,082,598	$ 877,314
Liabilities and Stockholders Equity		
Revolving notes	$ 210,387	$ 22,429
Accounts payable and accrued liabilities	219,708	204,793
Participation	11,849	11,453
Deferred income taxes	41,132	37,472
Deferred revenue	11,040	17,481
Notes payable	364,400	362,314
Subordinated debt	1,270	2,091
Minority interest	1,202	
Commitments and contingencies (Note 11)		
Stockholders equity:		
Preferred stock without par value; 25,000 shares authorized; none outstanding		
Common stock without par value; 50,000 shares authorized; 15,971 and 15,954 shares outstanding at November 30, 2006 and August 31, 2006	16	16
Additional paid-in capital	72,870	71,124
Retained earnings	149,134	148,542
Accumulated other comprehensive loss	(410)	(401)
	221,610	219,281
	$ 1,082,598	$ 877,314

The accompanying notes are an integral part of these statements.

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THE GREENBRIER COMPANIES, INC.

Consolidated Statements of Operations

(In thousands, except per share amounts, unaudited)

	Three Months Ended November 30, 2006	2005
Revenue		
Manufacturing	$ 168,692	$ 141,835
Refurbishment & parts	51,236	22,761
Leasing & services	26,695	21,766
	246,623	186,362
Cost of revenue		
Manufacturing	161,688	123,031
Refurbishment & parts	45,007	19,999
Leasing & services	10,811	10,439
	217,506	153,469
Margin	29,117	32,893
Other costs		
Selling and administrative expense	17,124	15,541
Interest and foreign exchange	9,641	4,573
	26,765	20,114
Earnings before income taxes, minority interest and equity in unconsolidated subsidiaries	2,352	12,779
Income tax expense	(580)	(4,934)
Earnings before minority interest and equity in unconsolidated subsidiaries	1,772	7,845
Minority interest	(2)	
Equity in earnings of unconsolidated subsidiaries	100	172
Net earnings	$ 1,870	$ 8,017
Basic earnings per common share:	$ 0.12	$ 0.52
Diluted earnings per common share:	$ 0.12	$ 0.51
Weighted average common shares:		
Basic	15,961	15,511
Diluted	16,010	15,847

The accompanying notes are an integral part of these statements.

THE GREENBRIER COMPANIES, INC.

Consolidated Statements of Cash Flows

(In thousands, unaudited)

	Three Months Ended November 30, 2006	Three Months Ended November 30, 2005
Cash flows from operating activities:		
Net earnings	$ 1,870	$ 8,017
Adjustments to reconcile net earnings to net cash provided by (used in) operating activities:		
Deferred income taxes	303	(1,122)
Depreciation and amortization	7,526	5,873
Gain on sales of equipment	(3,222)	(612)
Other	40	40
Decrease (increase) in assets (net of acquisitions):		
Accounts and notes receivable	(8,029)	31,228
Inventories	(1,379)	922
Assets held for sale	(15,342)	(43,619)
Other	351	(393)
Increase (decrease) in liabilities (net of acquisitions):		
Accounts payable and accrued liabilities	(17,547)	10,878
Participation	396	486
Deferred revenue	(6,906)	(2,846)
Net cash provided by (used in) operating activities	(41,939)	8,852
Cash flows from investing activities:		
Acquisitions, net of cash acquired	(264,470)	
Principal payments received under direct finance leases	229	871
Proceeds from sales of equipment	20,833	3,169
Investment in and advances to unconsolidated joint venture	137	75
Increase in restricted cash	(436)	
Capital expenditures	(30,458)	(44,401)
Net cash used in investing activities	(274,165)	(40,286)
Cash flows from financing activities:		
Changes in revolving notes	186,608	2,096
Proceeds (expenses) from notes payable	(69)	58,873
Repayments of notes payable	(931)	(1,382)
Repayments of subordinated debt	(821)	(1,442)
Proceeds from minority interest	1,200	
Stock options exercised and restricted stock awards	877	805
Excess tax benefit of stock options exercised	869	639
Net cash provided by financing activities	187,733	59,589

Effect of exchange rate changes	(164)	(664)
Increase (decrease) in cash and cash equivalents	(128,535)	27,491
Cash and cash equivalents		
Beginning of period	142,894	73,204
End of period	$ 14,359	$ 100,695
Cash paid during the period for:		
Interest	$ 11,929	$ 8,998
Income taxes	$ 48	$ 4,374

The accompanying notes are an integral part of these statements.

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THE GREENBRIER COMPANIES, INC.

	Three Months Ended November 30, 2006	2005
Supplemental disclosure of non-cash activity:		
Assumption of Rail Car America capital lease obligation	$ 119	$
Supplemental disclosure of acquisitions (See Note 2):		
Assets acquired, net of cash	$ (300,555)	$
Liabilities assumed	33,085	
Acquisition note payable	3,000	
Cash paid for acquisitions	267,523	
Cash acquired	$ 3,053	$

The accompanying notes are an integral part of these statements.

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Notes to Consolidated Financial Statements

(Unaudited)

Note 1 Interim Financial Statements

The Consolidated Financial Statements of The Greenbrier Companies, Inc. and Subsidiaries (Greenbrier or the Company) as of November 30, 2006 and for the three months ended November 30, 2006 and 2005 have been prepared without audit and reflect all adjustments (consisting of normal recurring accruals) which, in the opinion of management, are necessary for a fair presentation of the financial position and operating results for the periods indicated. The results of operations for the three months ended November 30, 2006 are not necessarily indicative of the results to be expected for the entire year ending August 31, 2007. Certain reclassifications have been made to the prior period s Consolidated Financial Statements to conform to the current year presentation.

Certain notes and other information have been condensed or omitted from the interim financial statements presented in this Quarterly Report on Form 10-Q. Therefore, these financial statements should be read in conjunction with the Consolidated Financial Statements contained in the Company s 2006 Annual Report on Form 10-K.

Management estimates The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires judgment on the part of management to arrive at estimates and assumptions on matters that are inherently uncertain. These estimates may affect the amount of assets, liabilities, revenue and expenses reported in the financial statements and accompanying notes and disclosure of contingent assets and liabilities within the financial statements. Estimates and assumptions are periodically evaluated and may be adjusted in future periods. Actual results could differ from those estimates.

Minority interest In October 2006, the Company formed a joint venture with Grupo Industrial Monclova (GIMSA) to build new railroad freight cars for the North American marketplace at GIMSA s existing manufacturing facility located in Monclova, Mexico. Each party maintains a 50% ownership. Production is anticipated to begin in our third quarter of 2007. The minority interest reflected in the Company s consolidated financial statements represents the joint venture partner s investment in this venture.

Assets Held for Sale Assets held for sale consist of new railcars in transit to delivery point, finished goods, railcars on lease with the intent to sell, used railcars that will either be sold or refurbished, placed on lease and then sold and completed wheel sets.

Initial Adoption of Accounting Policies In May 2005, the Financial Accounting Standards Board (FASB) issued SFAS No. 154, *Accounting Changes and Error Corrections* which replaces Accounting Principles Board (APB) opinion No. 20, *Accounting Changes* and SFAS No. 3, *Reporting Accounting Changes in Interim Financial Statements*. This statement requires retrospective application, unless impracticable, for changes in accounting principles in the absence of transition requirements specific to newly adopted accounting principles. This statement is effective for any accounting changes and corrections of errors made by the Company beginning September 1, 2006.

Prospective Accounting Changes In July 2006, the FASB issued FASB interpretation (FIN) No. 48, *Accounting for Uncertainties in Income Tax an Interpretation of FASB Statement No. 109,* This interpretation clarifies the accounting for uncertainties in income taxes. It prescribes a recognition and measurement threshold for financial statement disclosure of tax positions taken or expected to be taken on a tax return. This interpretation is effective for the Company for the fiscal year beginning September 1, 2007. Management has not yet determined the impact on the Consolidated Financial Statements.

Note 2 Acquisitions

On September 11, 2006, the Company purchased substantially all of the operating assets of Rail Car America (RCA), its American Hydraulics division and the assets of its wholly owned subsidiary, Brandon Corp. RCA, a leading provider of intermodal and conventional railcar repair services in North America, operates from four repair facilities throughout the United States. RCA also reconditions and repairs end-of-railcar cushioning units through its American Hydraulics division and operates a switching railroad in Nebraska through Brandon Corp. The purchase price of the net assets was $29.1 million in cash and a $3.0 million promissory note due in September 2008. The financial results since the acquisition are reported in the Company s consolidated financial statements as part of the refurbishment & parts segment. The impact of this acquisition was not material to the Company s results of operations, therefore, proforma financial information has not been included.

The allocation of the purchase price among certain assets and liabilities is still in process. As a result, the information shown below is preliminary and subject to further refinement upon completion of analyses.

The preliminary fair value of the net assets acquired from RCA was as follows:

(in thousands)

Accounts and notes receivable	$ 522
Inventories	7,937
Property, plant and equipment	22,066
Intangibles	3,719
Other	9
Total assets acquired	34,253
Accounts payable and accrued liabilities	1,985
Notes payable	119
Total liabilities assumed	2,104
Net assets acquired	$ 32,149

On November 6, 2006, the Company acquired 100% of the stock of Meridian Rail Holdings Corp. (Meridian) for $238.4 million in cash which includes the purchase price of $227.5 million plus preliminary working capital adjustments. Meridian is a leading supplier of wheel maintenance services to the North American freight car industry. Operating out of six facilities, Meridian supplies replacement wheel sets and axles to approximately 170 freight car maintenance locations where worn or damaged wheels, axles, or bearings are replaced. Meridian also performs coupler reconditioning and railcar repair at one of its facilities. The financial results since the acquisition are reported in the Company s consolidated financial statements as part of the refurbishment & parts segment.

The allocation of the purchase price among certain assets and liabilities is still in process. As a result, the information shown below is preliminary and subject to further refinement upon completion of analyses and valuations.

The preliminary fair value, based on historical costs, of the net assets acquired in the Meridian acquisition was as follows:

(in thousands)

Cash and cash equivalents	$ 3,053
Accounts and notes receivable	19,614
Inventories	50,029
Property, plant and equipment	15,154
Goodwill and intangibles	181,171
Other	334
Total assets acquired	269,355

Accounts payable and accrued liabilities	27,694
Deferred income taxes	3,287
Total liabilities assumed	30,981
Net assets acquired	$ 238,374

As a result of the preliminary allocation of the purchase price among assets and liabilities, Greenbrier recorded $172.5 million in goodwill.

The consolidated unaudited pro forma financial information below for the three months ended November 30, 2006 and 2005 was prepared as if the transaction to acquire Meridian had occurred at the beginning of each period presented:

	Three Months Ended November 30,	
(In thousands)	2006	2005
Revenue	$ 297,391	$ 232,137
Net earnings	$ 6,591	$ 10,250
Basic earnings per common share	$ 0.41	$ 0.66
Diluted earnings per common share	$ 0.41	$ 0.65

The unaudited pro forma financial information is not necessarily indicative of what actual results would have been had the transaction occurred at the beginning of the fiscal year, and it does not reflect the results of future operations of the Company.

Note 3 Inventories

(In thousands)	November 30, 2006	August 31, 2006
Supplies and raw materials	$ 107,091	$ 49,631
Work-in-process	110,157	118,555
Lower of cost or market adjustment	(7,971)	(5,035)
	$ 209,277	$ 163,151

Note 4 Warranty Accruals

Warranty costs are estimated and charged to operations to cover a defined warranty period. The estimated warranty cost is based on historical warranty claims for each particular product type. For new product types without a warranty history, preliminary estimates are based on historical information for similar product types. The accrual, included in accounts payable and accrued liabilities on the Consolidated Balance Sheet, is periodically reviewed and updated based on warranty trends.

Warranty accrual activity:

	Three Months Ended November 30,	
(In thousands)	2006	2005
Balance at beginning of period	$ 14,201	$ 15,037
Charged to cost of revenue	943	927
Payments	(670)	(1,060)
Currency translation effect	203	38
Acquisitions	1,824	
Balance at end of period	$ 16,501	$ 14,942

Note 5 Revolving Notes

All amounts originating in foreign currency have been translated at the November 30, 2006 exchange rate for the following discussion. Senior secured credit facilities aggregated $329.4 million as of November 30, 2006. Available borrowings are based on defined levels of inventory, receivables, and leased equipment, as well as total debt to consolidated capitalization and interest coverage ratios which at November 30, 2006 levels would provide for maximum borrowing of $280.1 million of which $210.4 million in revolving notes and $4.4 million in letters of credit are outstanding. A $290.0 million revolving line of credit is available through November 2011 to provide working capital and interim financing of equipment for the United States and Mexican operations. A $10.0 million line of credit is available through November 2011 for working capital for Canadian manufacturing operations. Advances under the U.S. and Canadian facilities bear interest at variable rates that depend on the type of borrowing and the defined ratio of debt to total capitalization. At November 30, 2006, there were $178.2 million and $3.9 million outstanding under the United States and Canadian credit facilities. Lines of credit totaling $29.4 million are available principally through June 2008 for working capital for the European manufacturing operation. The European credit facility had $28.3 million outstanding as of November 30, 2006.

In addition, the Company has a $25.0 million senior unsecured credit facility available through March 31, 2007. No amounts are outstanding under this credit facility.

Note 6 Comprehensive Income

The following is a reconciliation of net earnings to comprehensive income:

	Three Months Ended November 30,	
(In thousands)	2006	2005
Net earnings	$ 1,870	$ 8,017
Reclassification of derivative financial instruments recognized in net earnings during the three months (net of tax effect)	(399)	(1,251)
Unrealized gain on derivative financial instruments (net of tax effect)	37	923
Foreign currency translation adjustment (net of tax effect)	353	627
Comprehensive income	$ 1,861	$ 8,316

Accumulated other comprehensive loss, net of tax effect, consisted of the following:

(In thousands)	Unrealized Losses on Derivative Financial Instruments	Foreign Currency Translation Adjustment	Accumulated Other Comprehensive Loss
Balance, August 31, 2006	$ (18)	$ (383)	$ (401)
First quarter activity	(362)	353	(9)
Balance, November 30, 2006	$ (380)	$ (30)	$ (410)

Note 7 Earnings Per Share

The shares used in the computation of the Company s basic and diluted earnings per common share are reconciled as follows:

	Three Months Ended November 30,	
(In thousands)	2006	2005
Weighted average basic common shares outstanding	15,961	15,511
Dilutive effect of employee stock options	49	336
Weighted average diluted common shares outstanding	16,010	15,847

Weighted average diluted common shares outstanding include the incremental shares that would be issued upon the assumed exercise of stock options as calculated using the treasury stock method. No options were anti-dilutive for the three months ended November 30, 2006 and 2005.

Note 8 Stock Based Compensation

All stock options were vested prior to September 1, 2005 and accordingly no compensation expense was recorded for stock options for the three months ended November 30, 2006 and 2005. The value of stock awarded under restricted stock grants is amortized as compensation expense over the vesting period of two to five years. For the three months ended November 30, 2006 and 2005, $0.8 million and $0.6 million in compensation expense was recorded related to restricted stock grants.

Note 9 Derivative Instruments

Foreign operations give rise to market risks from changes in foreign currency exchange rates. Foreign currency forward exchange contracts with established financial institutions are utilized to hedge a portion of that risk in U.S. dollars, Pound Sterling and Euro. Interest rate swap agreements are utilized to reduce the impact of changes in interest rates on certain debt. The Company s foreign currency forward exchange contracts and interest rate swap agreements are designated as cash flow hedges, and therefore the unrealized gains and losses are recorded in accumulated other comprehensive loss.

Adjusting the contracts to the fair value of the cash flow hedges at November 30, 2006 resulted in an unrealized pre-tax loss of $4 thousand that was recorded in the line item accumulated other comprehensive loss and the fair value of the contracts is included in accounts payable and accrued liabilities on the Consolidated Balance Sheet. As the contracts mature at various dates through January 2007, any such gain or loss remaining will be recognized in manufacturing revenue along with the related transactions. In the event that the underlying sales transaction does not occur or does not occur in the period designated at the inception of the hedge, the amount classified in accumulated other comprehensive income (loss) would be reclassified to the current year s results of operations.

At November 30, 2006 exchange rates, interest rate swap agreements had a notional amount of $12.8 million and mature between May 2007 and March 2011. The fair value of these cash flow hedges at November 30, 2006 resulted in an unrealized pre-tax loss of $0.6 million. The loss is included in accumulated other comprehensive loss and the fair value of the contracts is included in accounts payable and accrued liabilities on the Consolidated Balance Sheet. As interest expense on the underlying debt is recognized, amounts corresponding to the interest rate swaps are reclassified from accumulated other comprehensive income (loss) and charged or credited to interest expense. At November 30, 2006 interest rates, approximately $0.1 million would be reclassified to interest expense in the next 12 months.

Note 10 Segment Information

Greenbrier has three reportable segments: manufacturing, refurbishment & parts and leasing & services. The acquisitions of Meridian and RCA during the current quarter resulted in the growth of the repair, refurbishment & parts portion of our business to the point that a new segment was added: refurbishment & parts. The results of this segment were previously aggregated in the manufacturing segment. The accounting policies of the segments are described in the summary of significant accounting policies in the Consolidated Financial Statements contained in the Company s 2006 Annual Report on Form 10-K. Performance is evaluated based on margin. Intersegment sales and transfers are accounted for at fair value as if the sales or transfers were to third parties. While intercompany transactions are treated like third-party transactions to evaluate segment performance, the revenues and related expenses are eliminated in consolidation and therefore do not impact consolidated results.

The information in the following table is derived directly from the segments internal financial reports used for corporate management purposes.

	Three Months Ended November 30,	
(In thousands)	2006	2005
Revenue:		
Manufacturing	$ 184,419	$ 207,029
Refurbishment & parts	53,014	23,365
Leasing & services	24,729	25,674
Intersegment eliminations	(15,539)	(69,706)
	$ 246,623	$ 186,362
Margin:		
Manufacturing	$ 7,004	$ 18,804
Refurbishment & parts	6,229	2,762
Leasing & services	15,884	11,327
	$ 29,117	$ 32,893

	November 30, 2006	August 31, 2006
Assets:		
Manufacturing	$ 310,542	293,754
Refurbishment & parts	397,627	48,340
Leasing & services	355,936	390,270
Unallocated	18,493	144,950
	$ 1,082,598	$ 877,314

Note 11 Commitments and Contingencies

From time to time, Greenbrier is involved as a defendant in litigation in the ordinary course of business, the outcome of which cannot be predicted with certainty. The most significant litigation is as follows:

On April 20, 2004, BC Rail Partnership initiated litigation against the Company in the Supreme Court of Nova Scotia, alleging breach of contract and negligent manufacture and design of railcars which were involved in a 1999 derailment. No trial date has been set.

On November 3, 2004, and November 4, 2004, in the District Court of Tarrant County, Texas, and in the District Court of Lancaster County, Nebraska, respectively, litigation was initiated against the Company by Burlington

Northern Santa Fe Railway (BNSF). BNSF alleges the failure of a supplier-provided component part on a railcar manufactured by Greenbrier in 1988, resulted in a derailment and a chemical spill. On June 24, 2006, the District Court of Tarrant County, Texas, entered an order granting the Company s motion for summary judgment as to all claims. On August 7, 2006, BNSF gave notice of appeal.

Greenbrier and a customer, SEB Finans AB (SEB), have raised performance concerns related to a component that the Company installed on 372 railcar units with an aggregate sales value of approximately $20.0 million produced under a contract with SEB. On December 9, 2005, SEB filed a Statement of Claim in an arbitration proceeding in Stockholm, Sweden, against Greenbrier alleging that the cars are defective and cannot be used for their intended purpose. SEB seeks damages in an undisclosed