

PARKER HANNIFIN CORP
Form 10-Q
November 06, 2008

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 September 30, 2008

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 1-4982

PARKER-HANNIFIN CORPORATION

(Exact name of registrant as specified in its charter)

OHIO
(State or other jurisdiction of
incorporation or organization)

34-0451060
(IRS Employer
Identification No.)

6035 Parkland Blvd., Cleveland, Ohio
(Address of principal executive offices)

44124-4141
(Zip Code)

Registrant's telephone number, including area code: (216) 896-3000

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 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):

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Large accelerated filer

Accelerated filer

Non-accelerated filer
(Do not check if a smaller

Smaller reporting company

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

Number of Common Shares outstanding at September 30, 2008 161,152,731

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

PARKER-HANNIFIN CORPORATION

CONSOLIDATED STATEMENT OF INCOME

(Dollars in thousands, except per share amounts)

(Unaudited)

	Three Months Ended September 30,	
	2008	2007
Net sales	\$ 3,064,688	\$ 2,787,256
Cost of sales	2,337,222	2,122,297
Gross profit	727,466	664,959
Selling, general and administrative expenses	332,683	324,961
Interest expense	28,096	22,421
Other expense (income), net	9,958	(165)
Income before income taxes	356,729	317,742
Income taxes	106,553	88,145
Net income	\$ 250,176	\$ 229,597
Earnings per share - basic	\$ 1.52	\$ 1.35
Earnings per share - diluted	\$ 1.50	\$ 1.33
Cash dividends per common share	\$.25	\$.21

See accompanying notes to consolidated financial statements.

PARKER-HANNIFIN CORPORATION

CONSOLIDATED BALANCE SHEET

(Dollars in thousands)

	(Unaudited) September 30, 2008	June 30, 2008
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 608,327	\$ 326,048
Accounts receivable, net	1,821,681	2,046,726
Inventories:		
Finished products	601,989	600,132
Work in process	696,264	682,816
Raw materials	208,540	211,746
	1,506,793	1,494,694
Prepaid expenses	72,870	82,326
Deferred income taxes	147,447	145,831
Total current assets	4,157,118	4,095,625
Plant and equipment	4,593,809	4,728,078
Less accumulated depreciation	2,737,979	2,801,556
	1,855,830	1,926,522
Goodwill	2,625,761	2,798,092
Intangible assets, net	986,759	1,020,609
Other assets	507,088	546,006
Total assets	\$ 10,132,556	\$ 10,386,854
LIABILITIES		
Current liabilities:		
Notes payable	\$ 677,890	\$ 118,864
Accounts payable, trade	836,873	961,886
Accrued payrolls and other compensation	319,561	433,070
Accrued domestic and foreign taxes	219,298	183,136
Other accrued liabilities	489,005	486,300
Total current liabilities	2,542,627	2,183,256
Long-term debt	1,878,933	1,952,452
Pensions and other postretirement benefits	482,895	491,935
Deferred income taxes	165,136	162,678
Other liabilities	319,097	337,562
Total liabilities	5,388,688	5,127,883
SHAREHOLDERS' EQUITY		
Serial preferred stock, \$.50 par value; authorized 3,000,000 shares; none issued		
Common stock, \$.50 par value; authorized 600,000,000 shares; issued 181,046,128 shares at September 30 and June 30	90,523	90,523
Additional capital	559,784	528,802
Retained earnings	5,595,284	5,387,836
Unearned compensation related to guarantee of ESOP debt		(4,951)
Deferred compensation related to stock options	2,073	2,112

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Accumulated other comprehensive (loss) income	(236,421)	117,642
	6,011,243	6,121,964
Less treasury shares, at cost:		
19,893,397 shares at September 30 and 13,331,126 shares at June 30	(1,267,375)	(862,993)
Total shareholders' equity	4,743,868	5,258,971
Total liabilities and shareholders' equity	\$ 10,132,556	\$ 10,386,854

See accompanying notes to consolidated financial statements.

PARKER-HANNIFIN CORPORATION

CONSOLIDATED STATEMENT OF CASH FLOWS

(Dollars in thousands)

(Unaudited)

	Three Months Ended September 30,	
	2008	2007
<u>CASH FLOWS FROM OPERATING ACTIVITIES</u>		
Net income	\$ 250,176	\$ 229,597
Adjustments to reconcile net income to net cash provided by operations:		
Depreciation	64,057	61,263
Amortization	22,109	14,913
Stock compensation	20,655	23,554
Deferred income taxes	7,622	(3,452)
Foreign currency transaction loss (gain)	1,159	(5,180)
Loss on sale of plant and equipment	765	1,003
Changes in assets and liabilities, net of effects from acquisitions:		
Accounts receivable	118,791	2,975
Inventories	(89,651)	(53,943)
Prepaid expenses	5,783	1,808
Other assets	8,305	13,735
Accounts payable, trade	(83,240)	(28,644)
Accrued payrolls and other compensation	(75,045)	(90,089)
Accrued domestic and foreign taxes	59,149	49,297
Other accrued liabilities	3,849	18,781
Pensions and other postretirement benefits	15,588	21,111
Other liabilities	(22,725)	12,172
Net cash provided by operating activities	307,347	268,901
<u>CASH FLOWS FROM INVESTING ACTIVITIES</u>		
Acquisitions (less acquired cash of \$119 in 2008 and \$177 in 2007)	(12,088)	(33,551)
Capital expenditures	(98,273)	(56,484)
Proceeds from sale of plant and equipment	7,437	1,544
Other	(8,004)	(8,188)
Net cash (used in) investing activities	(110,928)	(96,679)
<u>CASH FLOWS FROM FINANCING ACTIVITIES</u>		
Proceeds from exercise of stock options	532	9,416
(Payments for) common shares	(413,959)	(512,835)
Tax benefit from share-based compensation	2,837	7,377
Proceeds from notes payable, net	564,580	375,150
Proceeds from long-term borrowings	3,265	3,403
(Payments of) long-term borrowings	(6,287)	(4,532)
Dividends	(41,109)	(36,544)
Net cash provided by (used in) financing activities	109,859	(158,565)
Effect of exchange rate changes on cash	(23,999)	1,554
Net increase in cash and cash equivalents	282,279	15,211
Cash and cash equivalents at beginning of year	326,048	172,706
Cash and cash equivalents at end of period	\$ 608,327	\$ 187,917

See accompanying notes to consolidated financial statements.

PARKER-HANNIFIN CORPORATION

BUSINESS SEGMENT INFORMATION BY INDUSTRY

(Dollars in thousands)

(Unaudited)

The Company operates in three reportable business segments: Industrial, Aerospace and Climate & Industrial Controls. The Industrial Segment is the largest and includes a significant portion of international operations.

Industrial - This segment produces a broad range of motion-control and fluid systems and components used in all kinds of manufacturing, packaging, processing, transportation, mobile construction, agricultural and military machinery and equipment. Sales are made directly to major original equipment manufacturers (OEMs) and through a broad distribution network to smaller OEMs and the aftermarket.

Aerospace - This segment designs and manufactures products and provides aftermarket support for commercial, military and general aviation aircraft, missile and spacecraft markets. The Aerospace Segment provides a full range of systems and components for hydraulic, pneumatic and fuel applications.

Climate & Industrial Controls - This segment manufactures motion-control systems and components for use primarily in the refrigeration and air conditioning and transportation industries.

	Three Months Ended September 30,	
	2008	2007
Net sales		
Industrial:		
North America	\$ 1,107,077	\$ 1,005,828
International	1,223,192	1,100,888
Aerospace	478,473	427,290
Climate & Industrial Controls	255,946	253,250
Total	\$ 3,064,688	\$ 2,787,256
Segment operating income		
Industrial:		
North America	\$ 160,486	\$ 155,182
International	202,952	183,433
Aerospace	68,148	57,436
Climate & Industrial Controls	15,499	15,506
Total segment operating income	447,085	411,557
Corporate general and administrative expenses	40,374	45,309
Income from operations before interest expense and other	406,711	366,248
Interest expense	28,096	22,421
Other expense	21,886	26,085
Income before income taxes	\$ 356,729	\$ 317,742

PARKER-HANNIFIN CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Dollars in thousands, except per share amounts

1. Management representation

In the opinion of the management of the Company, the accompanying unaudited consolidated financial statements contain all adjustments (consisting of only normal recurring accruals) necessary to present fairly the financial position as of September 30, 2008, the results of operations for the three months ended September 30, 2008 and 2007 and cash flows for the three months then ended. These financial statements should be read in conjunction with the consolidated financial statements and related notes included in the Company's 2008 Annual Report on Form 10-K. Interim period results are not necessarily indicative of the results to be expected for the full fiscal year.

2. New accounting pronouncements

In December 2007, the Financial Accounting Standards Board (FASB) issued FASB Statement No. 141 (revised 2007), Business Combinations (Statement No. 141R). Statement No. 141R changes the accounting for business combinations both during the period of acquisition and in subsequent periods. Acquisition costs will generally be expensed as incurred; noncontrolling interests will be valued at fair value at the acquisition date; in-process research and development will be recorded at fair value as an indefinite-lived asset at the acquisition date; restructuring costs associated with a business combination will generally be expensed subsequent to the acquisition date; and changes in deferred tax asset valuation allowances and income tax uncertainties after the acquisition date generally will affect income tax expense. Statement No. 141R is effective for fiscal years beginning after December 15, 2008. Generally, the effect of Statement No. 141R on the Company's financial position or results of operations will depend on future acquisitions.

In December 2007, the FASB issued FASB Statement No. 160, Noncontrolling Interests in Consolidated Financial Statements—an amendment of ARB 51. Statement No. 160 requires the recognition of a noncontrolling interest as equity in the consolidated financial statements and separate from the parent's equity. The amount of net income attributable to the noncontrolling interest will be included in consolidated net income on the face of the income statement. Statement No. 160 is effective for fiscal years beginning after December 15, 2008. The Company has not yet determined the effect on the Company's financial position or results of operations of complying with the provisions of Statement No. 160.

In March 2008, the FASB issued FASB Statement No. 161, Disclosures about Derivative Instruments and Hedging Activities. Statement No. 161 establishes guidelines to report how derivative and hedging activities affect an entity's financial position, financial performance, and cash flows. Statement No. 161 is effective for fiscal years beginning after November 15, 2008. The Company has not yet determined the effect, if any, that Statement No. 161 will have on the Company's disclosures regarding derivatives and hedging activities.

3. Product warranty

In the ordinary course of business, the Company warrants its products against defect in design, materials and workmanship over various time periods. The warranty accrual as of September 30, 2008 and June 30, 2008 is immaterial to the financial position of the Company and the change in the accrual for both the current-year quarter and prior-year quarter was immaterial to the Company's results of operations and cash flows.

4. Earnings per share

The following table presents a reconciliation of the numerator and denominator of basic and diluted earnings per share for the three months ended September 30, 2008 and 2007.

	Three Months Ended September 30,	
	2008	2007
<u>Numerator:</u>		
Income applicable to common shares	\$ 250,176	\$ 229,597
<u>Denominator:</u>		
Basic - weighted average common shares	164,415,418	169,782,809
Increase in weighted average from dilutive effect of equity-based awards	2,497,798	3,438,683
Diluted - weighted average common shares, assuming exercise of equity-based awards	166,913,216	173,221,492
Basic earnings per share	\$ 1.52	\$ 1.35
Diluted earnings per share	\$ 1.50	\$ 1.33

At September 30, 2008 and 2007, 3,645,525 and 1,898,576 common shares, respectively, subject to equity-based awards were excluded from the computation of diluted earnings per share because the effect of their exercise would be anti-dilutive.

5. Share repurchase program

The Company has a program to repurchase its common shares. Under the program, the Company is authorized to repurchase an amount of common shares each fiscal year equal to the greater of 7.5 million shares or five percent of the shares outstanding as of the end of the prior fiscal year. Repurchases are funded primarily from operating cash flows, and the shares are initially held as treasury stock. The Company repurchased 6,708,024 shares of its common stock at an average price of \$61.71 during the three-month period ended September 30, 2008 under this program.

6. Comprehensive income

The Company's primary item of other comprehensive income (loss) is foreign currency translation adjustments. Comprehensive income for the three months ended September 30, 2008 and 2007 was as follows:

	Three Months Ended September 30,	
	2008	2007
Net income	\$ 250,176	\$ 229,597