

EXPEDITORS INTERNATIONAL OF WASHINGTON INC  
Form 10-Q  
May 07, 2012

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 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: 0-13468

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
(Exact name of registrant as specified in its charter)

Washington  
(State or other jurisdiction of  
incorporation or organization)

91-1069248  
(IRS Employer  
Identification Number)

1015 Third Avenue, 12<sup>th</sup>Floor, Seattle, Washington  
(Address of principal executive offices)  
(206) 674-3400

98104  
(Zip Code)

(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). 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  (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes  No

At May 2, 2012, the number of shares outstanding of the issuer's Common Stock was 212,405,452.

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## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIES

## Condensed Consolidated Balance Sheets

(In thousands, except share data)

(Unaudited)

	March 31, 2012	December 31, 2011
Current Assets:		
Cash and cash equivalents	\$1,412,915	\$1,294,356
Short-term investments	16,277	472
Accounts receivable, less allowance for doubtful accounts of \$9,805 at March 31, 2012 and \$10,381 at December 31, 2011	934,866	934,752
Deferred Federal and state income taxes	9,754	10,415
Other	36,386	46,888
Total current assets	2,410,198	2,286,883
Property and equipment, less accumulated depreciation and amortization of \$306,524 at March 31, 2012 and \$296,481 at December 31, 2011	550,323	538,806
Goodwill and other intangibles, net	10,215	10,557
Other assets, net	30,487	30,581
Total assets	\$3,001,223	\$2,866,827
Current Liabilities:		
Accounts payable	629,503	606,628
Accrued expenses, primarily salaries and related costs	170,535	169,445
Federal, state and foreign income taxes	28,219	20,072
Total current liabilities	828,257	796,145
Deferred Federal and state income taxes	70,932	60,613
Commitments and contingencies		
Shareholders' Equity:		
Preferred stock, none issued	—	—
Common stock, par value \$.01 per share. Issued and outstanding 212,275,083 shares at March 31, 2012 and 212,003,662 shares at December 31, 2011	2,123	2,120
Additional paid-in capital	18,338	13,260
Retained earnings	2,067,929	1,991,222
Accumulated other comprehensive income (loss)	7,064	(2,964)
Total shareholders' equity	2,095,454	2,003,638
Noncontrolling interest	6,580	6,431
Total equity	2,102,034	2,010,069
Total liabilities and equity	\$3,001,223	\$2,866,827
See accompanying notes to condensed consolidated financial statements.		

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIES

Condensed Consolidated Statements of Earnings

(In thousands, except share data)

(Unaudited)

	Three months ended	
	March 31,	
	2012	2011
Revenues:		
Airfreight services	\$638,912	\$700,923
Ocean freight and ocean services	434,336	440,141
Customs brokerage and other services	338,122	319,784
Total revenues	1,411,370	1,460,848
Operating Expenses:		
Airfreight consolidation	481,043	524,636
Ocean freight consolidation	331,954	339,549
Customs brokerage and other services	151,802	142,748
Salaries and related costs	246,132	237,815
Rent and occupancy costs	21,176	21,381
Depreciation and amortization	9,545	9,174
Selling and promotion	8,663	9,163
Other	35,784	29,152
Total operating expenses	1,286,099	1,313,618
Operating income	125,271	147,230
Other Income (Expense):		
Interest income	3,360	2,320
Interest expense	(620)	(214)
Other, net	1,097	1,117
Other income, net	3,837	3,223
Earnings before income taxes	129,108	150,453
Income tax expense	52,386	59,246
Net earnings	76,722	91,207
Less net earnings (losses) attributable to the noncontrolling interest	15	(25)
Net earnings attributable to shareholders	\$76,707	\$91,232
Diluted earnings attributable to shareholders per share	\$.36	\$.42
Basic earnings attributable to shareholders per share	\$.36	\$.43
Weighted average diluted shares outstanding	214,199,510	215,863,386
Weighted average basic shares outstanding	212,097,662	212,088,860

See accompanying notes to condensed consolidated financial statements.

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIES

Condensed Consolidated Statements of Comprehensive Income

(In thousands, except share data)

(Unaudited)

	Three months ended	
	March 31,	
	2012	2011
Net earnings	\$76,722	\$91,207
Other comprehensive income, net of tax:		
Foreign currency translation adjustments, net of tax of \$5,499 and \$4,841 for the three months ended March 31, 2012 and 2011	10,162	8,821
Other comprehensive income	10,162	8,821
Comprehensive income	86,884	100,028
Less comprehensive income (loss) attributable to the noncontrolling interest	149	(37 )
Comprehensive income attributable to shareholders	\$86,735	\$100,065

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

	Three months ended		
	March 31,		
	2012	2011	
Operating Activities:			
Net earnings	\$76,722	\$91,207	
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Provision for losses on accounts receivable	(467	) 1,853	
Deferred income tax expense (benefit)	5,481	(1,936	)
Excess tax benefits from stock plans	(3,426	) (2,246	)
Stock compensation expense	10,600	10,472	
Depreciation and amortization	9,545	9,174	
Gain on sale of assets	(65	) (30	)
Other	282	307	
Changes in operating assets and liabilities:			
Decrease in accounts receivable	12,968	6,683	
Decrease (increase) in other current assets	1,924	(1,415	)
Increase in accounts payable and accrued expenses	13,559	30,187	
Increase in income taxes payable, net	20,274	33,577	
Net cash provided by operating activities	147,397	177,833	
Investing Activities:			
Increase in short-term investments, net	(15,780	) (89	)
Purchase of property and equipment	(17,088	) (21,125	)
Proceeds from sale of property and equipment	112	43	
Other	358	(1,442	)
Net cash used in investing activities	(32,398	) (22,613	)
Financing Activities:			
Proceeds from issuance of common stock	12,920	7,804	
Repurchases of common stock	(21,865	) (19,584	)
Excess tax benefits from stock plans	3,426	2,246	
Net cash used in financing activities	(5,519	) (9,534	)
Effect of exchange rate changes on cash and cash equivalents	9,079	8,320	
Increase in cash and cash equivalents	118,559	154,006	
Cash and cash equivalents at beginning of period	1,294,356	1,084,465	
Cash and cash equivalents at end of period	\$1,412,915	\$1,238,471	
Interest and Taxes Paid:			
Interest	\$187	\$4	
Income taxes	26,512	26,276	

See accompanying notes to condensed consolidated financial statements.

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.  
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(in thousands, except share data)

(Unaudited)

Note 1. Summary of Significant Accounting Policies

A. Basis of Presentation

Expeditors International of Washington, Inc. (“the Company”) is a non-asset based provider of global logistics services operating through a worldwide network of offices and exclusive or non-exclusive agents. The Company’s customers include retailing and wholesaling, electronics, and manufacturing companies around the world.

The condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. As a result, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP) have been condensed or omitted. The Company believes that the disclosures made are adequate to make the information presented not misleading. The condensed consolidated financial statements reflect all adjustments, consisting of normal recurring items, which are, in the opinion of management, necessary to a fair statement of the results for the interim periods presented. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes included in the Company’s Form 10-K as filed with the Securities and Exchange Commission on February 28, 2012. Certain 2011 amounts have been reclassified to conform with the 2012 presentation. All dollar amounts in the notes are presented in thousands except for share data. All significant intercompany accounts and transactions have been eliminated in consolidation.

B. Accounts Receivable

The Company maintains an allowance for doubtful accounts, which is reviewed at least monthly for estimated losses resulting from the inability of its customers to make required payments for services and advances. Additional allowances may be necessary in the future if the ability of its customers to pay deteriorates. The Company has recorded an allowance for doubtful accounts in the amounts of \$9,805 as of March 31, 2012 and \$10,381 as of December 31, 2011. Additions and write-offs have not been significant in the periods presented.

C. Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of the assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. The Company uses estimates primarily in the following areas: accounts receivable valuation, accrual of costs related to ancillary services the Company provides, accrual of insurance liabilities for the portion of the freight related exposure which the Company has self-insured, accrual of various tax liabilities, accrual of loss contingencies and calculation of share-based compensation expense. Actual results could differ from those estimates.

D. Recent Accounting Pronouncements

In June 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2011-No. 05 “Presentation of Comprehensive Income”, which amends Accounting Standards Codification (ASC) Topic 220 -“Comprehensive Income”. This update is intended to increase the prominence of items reported in other comprehensive income by giving the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The Company adopted the provisions of ASU 2011-No. 05, as amended by ASU 2011-No. 12, beginning in the first quarter of 2012. Accordingly, condensed consolidated statements of comprehensive income were included consecutive to the condensed consolidated statements of earnings. The adoption only had a presentation impact on the Company's consolidated financial statements.

Note 2. Share-Based Compensation

The Company provides compensation benefits by granting stock options and employee stock purchase rights to its employees and restricted shares to its directors. The Company recognizes stock compensation expense based on an

estimate of the fair value of awards granted to employees and directors under the Company's stock option, director restricted stock and employee stock purchase rights plans. The expense, adjusted for expected forfeitures, is recognized on a straight-line basis over the stock awards' vesting period. The forfeiture assumption used to calculate compensation expense is primarily based on

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historical pre-vesting employee forfeiture patterns.

The Company's annual grant of option awards generally takes place during the second quarter of each fiscal year and no grants were made in the quarters ended March 31, 2012 and 2011. The grant of employee stock purchase rights and the issuance of shares under the employee stock purchase plan are made in the third quarter of each fiscal year and none were issued in the quarters ended March 31, 2012 and 2011.

Total stock compensation expense and the total related tax benefit recognized are as follows:

	Three months ended March 31,	
	2012	2011
Stock compensation expense	\$10,600	\$10,472
Recognized tax benefit	\$39	\$38

### Note 3. Basic and Diluted Earnings per Share

The following table reconciles the numerator and the denominator of the basic and diluted per share computations for earnings attributable to shareholders per share:

(Amounts in thousands, except share and per share amounts)	Three months ended March 31,		Earnings per share
	Net earnings attributable to shareholders	Weighted average shares	
2012			
Basic earnings attributable to shareholders	\$76,707	212,097,662	\$ .36
Effect of dilutive potential common shares	—	2,101,848	—
Diluted earnings attributable to shareholders	\$76,707	214,199,510	\$ .36
2011			
Basic earnings attributable to shareholders	\$91,232	212,088,860	\$ .43
Effect of dilutive potential common shares	—	3,774,526	—
Diluted earnings attributable to shareholders	\$91,232	215,863,386	\$ .42

The following shares have been excluded from the computation of diluted earnings per share because the effect would have been antidilutive:

	Three months ended March 31,	
	2012	2011
Shares	7,359,424	4,564,830

## Note 4. Components of Equity

The components of equity for the three months ended 2012 and 2011 are as follows:

	Shareholders' equity	Noncontrolling interest	Total equity
Balance at December 31, 2011	\$2,003,638	6,431	2,010,069
Exercise of stock options	12,920	—	12,920
Shares repurchased under provisions of stock repurchase plans	(21,865 )	—	(21,865 )
Stock compensation expense	10,600	—	10,600
Tax benefits from stock plans	3,426	—	3,426
Net earnings	76,707	15	76,722
Other comprehensive income	10,028	134	10,162
Balance at March 31, 2012	\$2,095,454	6,580	2,102,034
Balance at December 31, 2010	\$1,740,906	7,248	1,748,154
Exercise of stock options	7,804	—	7,804
Shares repurchased under provisions of stock repurchase plans	(19,584 )	—	(19,584 )
Stock compensation expense	10,472	—	10,472
Tax benefits from stock plans	2,246	—	2,246
Net earnings	91,232	(25 )	91,207
Other comprehensive income (loss)	8,833	(12 )	8,821
Balance at March 31, 2011	\$1,841,909	7,211	1,849,120

Subsequent to the end of the quarter, on May 2, 2012, the Board of Directors declared a semi-annual cash dividend of \$0.28 per share payable on June 15, 2012 to shareholders of record as of June 1, 2012.

## Note 5. Fair Value of Financial Instruments

The Company's financial instruments, other than cash, consist primarily of cash equivalents, short-term investments, accounts receivable, accounts payable and accrued expenses. The carrying value of these financial instruments approximates their fair value. Cash equivalents consist of highly liquid investments with a maturity of three months or less at date of purchase. Short term investments have a maturity of greater than three months at date of purchase.

Cash, cash equivalents and short-term investments consist of the following:

	March 31, 2012		December 31, 2011	
	Cost	Fair Value	Cost	Fair Value
Cash and Cash Equivalents:				
Cash and overnight deposits	\$444,914	\$444,914	\$445,586	\$445,586
Corporate commercial paper	853,302	853,734	791,729	791,902
Time deposits	114,699	114,699	57,041	57,041
Total cash and cash equivalents	1,412,915	1,413,347	1,294,356	1,294,529
Short-Term Investments:				
Time deposits	16,277	16,277	472	472
Total	\$1,429,192	\$1,429,624	\$1,294,828	\$1,295,001

The fair value of corporate commercial paper is based on the use of market interest rates for identical or similar assets.

## Note 6. Contingencies

On October 10, 2007, the U. S. Department of Justice (DOJ) issued a subpoena ordering the Company to produce certain information and records relating to an investigation of alleged anti-competitive behavior amongst air cargo freight forwarders. As part of this process, the Company has met with and continues to co-operate with the DOJ. The Company may incur additional costs during the course of this ongoing investigation, which could include fines and/or penalties if the DOJ concludes that the Company has engaged in anti-competitive behavior and such fines and/or penalties could have a material impact on the Company's results of operations and operating cash flows for any particular quarter or year.

On April 19, 2012, the Company received a federal grand jury subpoena from the DOJ requiring the production of



documents related to the export or re-export by unaffiliated third-parties to end users in a US-embargoed country of products and/or services produced by a U.S. manufacturer. In a related matter, the Company is also responding to an administrative subpoena from the Commerce Department's Bureau of Industry and Security (BIS) requiring the production of documents pertaining to the export or re-export of US-origin goods to the same embargoed country. The Company is co-operating with the DOJ and BIS. If it is determined that the Company or one of its subsidiaries, directly or indirectly, facilitated the export or re-export of these specified products and/or services, the Company may incur fines and/or penalties which could have a material impact on the Company's results of operations and cash flows for any particular quarter or year.

On February 10, 2010, the Company and its Hong Kong subsidiary, Expeditors Hong Kong Limited, received a Statement of Objections (SO) from the European Commission (EC). The SO initiated a proceeding against the Company alleging anti-competitive behavior contrary to European Union rules on competition. Specific to the Company, the allegations in the SO are limited to Peak Season Surcharge (PSS) for the period from August 2005 to June 2006 and only concern airfreight trade lanes between South China/Hong Kong and the European Economic Area. On March 28, 2012, the EC concluded that the Company engaged in anti-competitive behavior and fined the Company €4.14 million (\$5.5 million). This fine was recorded in March 2012 and is included in other operating expenses.

Government investigations are subject to inherent uncertainties, and unfavorable rulings could occur. An unfavorable ruling could include substantial monetary damages and, in matters in which injunctive relief or other conduct remedies are sought, an injunction or other order relating to business conduct. Were unfavorable final outcomes to occur, the Company's results of operations and cash flows for the particular quarter or year could be materially harmed.

The Company is involved in other claims and lawsuits which arise in the ordinary course of business, none of which currently, in management's opinion, are expected to have a significant effect on the Company's operations or financial position. As of March 31, 2012, the amounts accrued for these claims and lawsuits, and the other legal matters described above, are not significant to the Company's operations or financial position. At this time the Company is unable to estimate any additional loss or range of reasonably possible loss, if any, beyond the amounts recorded, that might result from the resolution of these matters.

#### Note 7. Business Segment Information

The Company is organized functionally in geographic operating segments. Accordingly, management focuses its attention on revenues, net revenues, operating income, identifiable assets, capital expenditures, depreciation and amortization and equity generated in each of these geographical areas when evaluating the effectiveness of geographic management. The Company charges its subsidiaries and affiliates for services rendered in the United States on a cost recovery basis. Transactions among the Company's various offices are conducted using the same arms-length pricing methodologies the Company uses when its offices transact business with independent agents.

Financial information regarding the Company's operations by geographic area are as follows:

(in thousands)	UNITED STATES	OTHER NORTH AMERICA	LATIN AMERICA	ASIA PACIFIC	EUROPE and AFRICA	MIDDLE EAST and INDIA	ELIMI-NATIONS	CONSOLI-DATED
Three months ended March 31, 2012:								
Revenues from unaffiliated customers	\$377,302	49,954	19,269	688,070	206,271	70,504	—	1,411,370
Transfers between geographic areas	22,208	2,465	5,079	10,972	9,467	4,651	(54,842 )	—
Total revenues	\$399,510	52,419	24,348	699,042	215,738	75,155	(54,842 )	1,411,370
Net revenues	\$181,475	22,242	14,835	131,814	71,533	24,672	—	446,571
Operating income	\$45,525	6,369	4,762	47,238	14,247	7,130	—	125,271
Identifiable assets at quarter end	\$1,590,900	96,312	52,214	708,528	404,839	149,416	(986 )	3,001,223
Capital expenditures	\$9,759	176	255	5,287	942	669	—	17,088
Depreciation and amortization	\$5,622	187	217	1,624	1,404	491	—	9,545
Equity	\$1,315,321	56,341	31,060	471,498	164,165	93,282	(29,633 )	2,102,034
Three months ended March 31, 2011:								
Revenues from unaffiliated customers	\$377,106	43,846	20,332	728,130	213,612	77,822	—	1,460,848
Transfers between geographic areas	23,965	2,682	5,621	9,183	10,707	4,209	(56,367 )	—
Total revenues	\$401,071	46,528	25,953	737,313	224,319	82,031	(56,367 )	1,460,848
Net revenues	\$177,934	20,701	15,103	141,487	73,926	24,764	—	453,915
Operating income	\$53,734	5,789	4,763	59,438	17,707	5,799	—	147,230
Identifiable assets at quarter end	\$1,427,414	86,371	57,960	659,352	452,675	153,236	(276 )	2,836,732
Capital expenditures	\$4,030	160	156	4,712				