LIFETIME BRANDS, INC
Form 10-Q
August 09, 2006

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 June 30, 2006

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM ________ TO ________

LIFETIME BRANDS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**11-2682486**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

One Merrick Avenue, Westbury, New York, 11590
(Address of principal executive offices, including Zip Code)

(Registrant s telephone number, including area code) (**516) 683-6000**

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, 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 Accelerated filer Non-accelerated filer

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

The number of shares of the registrant s common stock outstanding as of August 1, 2006 was 13,469,000.

LIFETIME BRANDS, INC.
FORM 10-Q
FOR THE QUARTER ENDED JUNE 30, 2006

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PART 1. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

LIFETIME BRANDS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except share data)

	June 30, 2006 (unaudited)	December 31, 2005
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 168	$ 786
Accounts receivable, less allowances of $5,465 in 2006 and $7,913 in 2005	37,421	49,158
Inventories	137,081	91,953
Prepaid expenses	5,586	2,668
Deferred income taxes	5,787	7,703
Other current assets	4,300	3,482
TOTAL CURRENT ASSETS	190,343	155,750
PROPERTY AND EQUIPMENT, net	33,789	23,989
GOODWILL	40,877	16,200
OTHER INTANGIBLES, net	20,429	24,064
OTHER ASSETS	5,588	2,645
TOTAL ASSETS	$ 291,026	$ 222,648
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES		
Short-term borrowings	$ 7,700	$ 14,500
Accounts payable	12,851	17,397
Accrued expenses	28,476	28,694
Income taxes payable	--	9,316
TOTAL CURRENT LIABILITIES	49,027	69,907
DEFERRED RENT AND OTHER LONG-TERM LIABILITIES	4,882	2,287
DEFERRED INCOME TAX LIABILITIES	5,331	4,967
LONG-TERM DEBT	5,000	5,000
CONVERTIBLE NOTES	75,000	--
STOCKHOLDERS' EQUITY		
Common Stock, $.01 par value, shares authorized: 25,000,000; shares issued and outstanding: 13,469,000 in 2006 and 12,921,795 in 2005	134	129
Paid-in capital	115,841	101,468
Retained earnings	35,811	38,890
TOTAL STOCKHOLDERS' EQUITY	151,786	140,487
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 291,026	$ 222,648

See accompanying independent registered public accounting firm review report and notes to unaudited condensed consolidated financial statements.

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LIFETIME BRANDS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	**2005**	**2006**	**2005**
Net sales	$ 84,051	$ 46,154	$ 158,472	$ 89,272
Cost of sales	47,836	26,959	89,343	51,859
Distribution expenses	11,257	5,807	21,849	11,923
Selling, general and administrative expenses	26,549	10,940	47,119	21,239
Income (loss) from operations	(1,591)	2,448	161	4,251
Interest expense	827	291	1,133	490
Other (income) expense, net	32	(13)	31	(26)
Income (loss) before income taxes	(2,450)	2,170	(1,003)	3,787
Tax provision (benefit)	(943)	825	(392)	1,439
NET INCOME (LOSS)	$ (1,507)	$ 1,345	$ (611)	$ 2,348
BASIC AND DILUTED INCOME (LOSS) PER COMMON SHARE	$ (0.11)	$ 0.12	$ (0.05)	$ 0.21
WEIGHTED AVERAGE SHARES - BASIC	13,324	11,062	13,137	11,057
WEIGHTED AVERAGE SHARES AND COMMON SHARE EQUIVALENTS - DILUTED	13,324	11,288	13,137	11,277

See accompanying independent registered public accounting firm review report and notes to unaudited condensed consolidated financial statements.

LIFETIME BRANDS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(unaudited)

	Six Months Ended June 30, 2006	Six Months Ended June 30, 2005
OPERATING ACTIVITIES		
Net income (loss)	$ (611)	$ 2,348
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	3,522	2,159
Deferred income taxes	2,280	(92)
Deferred rent	92	(76)
Provision for losses on accounts receivable	--	111
Reserve for sales returns and allowances	5,952	3,767
Director stock grant	50	--
Stock compensation expense	330	--
Changes in operating assets and liabilities (excluding the effects of the acquisition of Syratech):		
Accounts receivable	22,483	5,768
Merchandise inventories	(19,494)	(8,583)
Prepaid expenses, other current assets and other assets	(5,988)	(1,005)
Accounts payable, trade acceptances, accrued expenses and other liabilities	(19,421)	(1,856)
Income tax payable	(9,001)	(1,773)
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	(19,806)	768
INVESTING ACTIVITIES		
Purchase of property and equipment	(3,928)	(2,966)
Purchase of Syratech, net of cash acquired of $509	(43,742)	--
NET CASH USED IN INVESTING ACTIVITIES	(47,670)	(2,966)
FINANCING ACTIVITIES		
Proceeds from (repayments of) short-term borrowings, net	(3,988)	1,900
Proceeds from exercise of stock options	107	195
Proceeds from issuance of convertible notes	72,188	--
Excess tax benefits from stock compensation	387	--
Payment of capital lease obligations	(188)	(154)
Cash dividends paid	(1,648)	(1,379)
NET CASH PROVIDED BY FINANCING ACTIVITIES	66,858	562
DECREASE IN CASH AND CASH EQUIVALENTS	(618)	(1,636)
Cash and cash equivalents at beginning of period	786	1,741
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 168	$ 105

See accompanying independent registered public accounting firm review report and notes to unaudited condensed consolidated financial statements.

LIFETIME BRANDS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2006
(unaudited)

Note A Basis of Presentation and Summary Accounting Policies

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments, consisting only of normal recurring accruals, considered necessary for a fair presentation have been included. Operating results for the three and six-month periods ended June 30, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006. It is suggested that these condensed consolidated financial statements be read in conjunction with the consolidated financial statements and footnotes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2005.

The Company s business and working capital needs are highly seasonal, with a majority of sales occurring in the third and fourth quarters. For the years ended December 31, 2005, 2004 and 2003, net sales for the third and fourth quarters accounted for 71%, 63% and 66% of total annual net sales, respectively. Moreover, operating profits earned in the third and fourth quarters accounted for 83%, 92% and 97% of total annual operating profits, respectively. Inventory levels increase primarily in the June through October time period in anticipation of the pre-holiday shipping season.

Revenue Recognition

The Company sells products wholesale to retailers and distributors and retail direct to the consumer through Company-operated outlet stores, catalog and Internet operations. Wholesale sales are recognized when title passes to and the risks and rewards of ownership have transferred to the customer. Outlet store sales are recognized at the time of sale, while catalog and Internet sales are recognized upon receipt by the customer. Shipping and handling fees that are billed to customers in sales transactions are recorded in net sales. Included in net sales for the three and six months ended June 30, 2006 is shipping and handling fee income generated from the Company s catalog and Internet business of $0.8 million and $1.8 million, respectively. The Company did not recognize any shipping and handling fee income for the three and six months ended June 30, 2005.

Distribution Expenses

Distribution expenses consist primarily of warehousing expenses, handling costs of products sold and freight-out. Freight-out costs included in distribution expenses amounted to $2.0 million and $1.0 million for the three months ended June 30, 2006 and 2005, respectively and $3.9 million and $2.1 million for the six months ended June 30, 2006 and 2005.

Earnings (Loss) Per Share

Basic earnings (loss) per share has been computed by dividing net income by the weighted average number of common shares outstanding. Diluted earnings (loss) per share adjusts basic earnings per share for the effects of all dilutive potential shares outstanding, only in the periods in which the effects are dilutive. The computation of weighted average dilutive shares outstanding for the three and six months ended June 30, 2006 excludes options to purchase 1,434,100 shares of common stock and 2,678,571 shares issuable upon the conversion of the Company s 4.75% Convertible Notes. These shares were excluded due to their antidilutive effect as a result of the Company s loss during these periods. The weighted average number of shares used in calculating diluted earnings per share for the three and six months ended June 30, 2005 includes the dilutive effect of stock options of 226,000 and 220,000 shares, respectively.

LIFETIME BRANDS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2006
(unaudited)

Note A Basis of Presentation and Summary Accounting Policies (continued)

New accounting pronouncement

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation (FIN) No. 48. FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with FASB Statement No. 109, Accounting for Income Taxes . FIN No. 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN No. 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN No. 48 is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the impact of FIN No. 48 on its consolidated financial statements.

Note B Stock Compensation

In June 2000, the stockholders of the Company approved the 2000 Long-Term Incentive Plan (the Plan), whereby up to 1,750,000 shares of common stock could be granted in the form of stock options or other equity-based awards to directors, officers, employees, consultants and service providers to the Company and its affiliates. In June 2006, the stockholders of the Company approved an amendment to the Plan to increase the number of shares of the Company s common stock available for grant under the Plan by 750,000 shares to 2,500,000 shares, and re-approved the performance criteria which may be utilized in establishing specific targets to be attained as a condition to the vesting of one or more stock-based awards under the Plan so as to qualify the compensation attributable to those awards as performance-based compensation under Section 162(m) of the Internal Revenue Code. The Plan authorizes the Board of Directors of the Company, or a duly appointed committee thereof, to issue incentive stock options as defined in Section 422 of the Internal Revenue Code, stock-based awards that do not conform to the requirements of Section 422 of the Code, and other stock-based awards. Options that have been granted under the Plan expire over a range of five to ten years from the date of the grant and vest over a range of up to five years from the date of grant. As of June 30, 2006, 668,180 shares were available for grant under the Plan. All options granted through June 30, 2006 under the Plan have exercise prices equal to the market value of the Company s stock on the date of grant.

A summary of the Company s stock option activity and related information for the six months ended June 30, 2006 is as follows:

	Options	Weighted-Average Exercise Price	Weighted average remaining contractual life (years)	Aggregate intrinsic value
Options outstanding, December 31, 2005	875,157	$ 14.51		
Grants	695,500	29.96		
Exercises	(136,557)	6.85		
Canceled	--			
Options outstanding June 30, 2006	1,434,100	22.73	6.70	$ 5,142,220
Options exercisable June 30, 2006	738,600	15.93	5.43	$ 5,142,220

LIFETIME BRANDS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2006
(unaudited)

Note B Stock Compensation (continued)

The aggregate intrinsic values in the table above represents the total pre-tax intrinsic value that would have been received by the option holders had all option holders exercised their options on June 30, 2006. The intrinsic value is calculated as the difference between the Company s closing stock price on the last trading day of the second quarter of fiscal 2006 and the exercise price, multiplied by the number of in-the-money options.

The total intrinsic value of options exercised for the six months ended June 30, 2006 was $2.5 million. The intrinsic value of options exercised is calculated as the difference between the market value of the Company s Common Stock at the date of exercise and the exercise price of the option.

Effective January 1, 2006, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 123(R), Share Based Payment . SFAS 123(R) requires that the expense resulting from all share-based payment transactions be recognized in the financial statements. SFAS 123(R) also requires that excess tax benefits associated with share-based payments be classified as a financing activity in the statement of cash flows, rather than as operating cash flows as required by previous accounting standards. The Company adopted SFAS 123(R) using the modified-prospective transition method. Accordingly, the Company has not restated prior period amounts.

In 2005, the Company accelerated the vesting of all unvested outstanding employee stock options in order to reduce the non-cash compensation expense that otherwise would have been required to be recorded under SFAS 123(R).

During the six months ended June 30, 2006, the Company recorded, as a component of selling general and administrative expenses, an expense of $330,000 for stock options granted during the period. The following illustrates the impact of expensing stock options on the Company s income from operations, net loss and earnings per share for the six months ended June 30, 2006:

(in thousands, except per share data)	Six months ended June 30, 2006
Decrease in income from operations	$ (330)
Increase in net loss	263
Increase in basic and diluted loss per share	0.02

Total unrecognized compensation cost related to unvested stock options at June 30, 2006 before the effect of income taxes was $6.7 million and is expected to be recognized over a weighted average period of 4.01 years.

The Company values its options using the Black-Scholes option valuation model. The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options, which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company s employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management s opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

The weighted average fair value of options granted during the six months ended June 30, 2006 was $12.11 per share.

LIFETIME BRANDS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2006
(unaudited)

Note B Stock Compensation (continued)

The fair value for these options was estimated at the date of grant using the following weighted-average assumptions:

Volatility	40.6%	(1)
Expected term (years)	5.17	(2)
Risk-free interest rate	5.02%	(3)
Expected dividend yield	0.834%	(4)

(1) Volatility is measured using historical volatility.

(2) The expected term represents the period of time for which the options granted are expected to be outstanding.

(3) The risk-free interest rate is based on United States treasury yields in effect at the time of grant corresponding to the expected term of the options.

(4) The expected dividend yield is based on the expected annual dividends and the market value of the Company s Common Stock on the grant date.

Prior to the adoption of SFAS 123(R) the Company accounted for options under the recognition and measurement principles of Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees , and related interpretations. Accordingly, for the periods prior to the adoption of SFAS 123(R), no stock-based employee compensation cost was reflected in net income as all options granted under the plan had exercise prices equal to the market values of the underlying common stock on the dates of grant. Pro-forma information regarding the impact of stock-based compensation on net income and income per share for prior periods is required by SFAS No. 123(R).

The following table illustrates what would have been the effect on net income and net income per share if the Company had accounted for its employee stock options using the fair value method during the three and six months ended June 30, 2005:

	Three months Ended June 30, 2005	**Six Months Ended June 30, 2005**
(in thousands, except per share data)		
Net income as reported	$ 1,345	$ 2,348
Deduct: Total stock option employee compensation expense determined under fair value based method for all awards, net of related tax effects	(34)	(68)
Pro forma net income	$ 1,311	$ 2,280
Income per common share:		
Basic and diluted - as reported	$ 0.12	$ 0.21
Basic and diluted - pro forma	$ 0.12	$ 0.20

LIFETIME BRANDS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
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Note C Credit Facility

The Company has a $100 million secured credit facility (the Credit Facility) that expires in July 2010. Borrowings under the Credit Facility are secured by all of the assets of the Company. Under the terms of the Credit Facility, the Company is required to satisfy certain financial covenants, including limitations on indebtedness and sale of assets; a minimum fixed charge ratio; a maximum leverage ratio and maintenance of a minimum net worth. At June 30, 2006, the Company was in compliance with these covenants. Borrowings under the Credit Facility have different interest rate options that are based either on an alternate base rate, the LIBOR rate or the lender s cost of funds rate, plus in each case a margin based on the leverage ratio.

As of June 30, 2006, the Company had $3.9 million of letters of credit and $7.7 million of short-term borrowings and a $5.0 million term loan outstanding under its Credit Facility, and as a result, the availability under the Credit Facility at June 30, 2006 was $83.4 million. The $5.0 million long-term loan is non-amortizing, bears interest at 6.07% and matures in August 2009. Interest rates on short-term borrowings at June 30, 2006 ranged from 5.40% to 6.38%.

Note D Convertible Debt

In June 2006, the Company issued $75 million aggregate principal amount of 4.75% Convertible Senior Notes due 2011 (the Notes). The Company used the proceeds from the Notes to repay outstanding borrowings under the Company s Credit Facility. The Notes are convertible into shares of the Company s Common Stock at a conversion price of $28.00 per share, subject to adjustment in certain events. The Notes bear interest at 4.75% per annum, payable semiannually in arrears on January 15 and July 15 of each year and are unsubordinated except with respect to the Company s debt to the extent secured by the Company s assets. The Notes mature on July 15, 2011.

The Notes are convertible at the option of the holder anytime prior to the close of business on the business day prior to the maturity date. Upon conversion, the Company may elect to deliver either shares of the Company s Common Stock, cash or a combination of cash and shares of the Company s Common Stock in satisfaction of the Company s obligations upon conversion of the Notes. At any time prior to the 26th trading day preceding the maturity date, the Company may irrevocably elect to satisfy in cash the Company s conversion obligation with respect to the principal amount of the Notes to be converted after the date of such election, with any remaini