

INGLES MARKETS INC  
Form 10-Q  
February 04, 2016

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 December 26, 2015

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 0-14706.

INGLES MARKETS, INCORPORATED

(Exact name of registrant as specified in its charter)

North Carolina (State or other jurisdiction of incorporation or organization)	56-0846267 (I.R.S. Employer Identification No.)
P.O. Box 6676, Asheville NC (Address of principal executive offices)	28816 (Zip Code)

(828) 669-2941

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 definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Edgar Filing: INGLES MARKETS INC - Form 10-Q

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 Exchange Act).

Yes No .

As of February 2, 2016, the Registrant had 13,942,826 shares of Class A Common Stock, \$0.05 par value per share, outstanding and 6,316,950 shares of Class B Common Stock, \$0.05 par value per share, outstanding.

1

---

INGLES MARKETS, INCORPORATED

INDEX

	Page No.
Part I – Financial Information	
Item 1. Financial Statements (Unaudited)	
Condensed Consolidated Balance Sheets as of December 26, 2015 and September 26, 2015	3
Condensed Consolidated Statements of Income for the Three Months Ended December 26, 2015 and December 27, 2014	4
Condensed Consolidated Statements of Changes in Stockholders’ Equity for the Three Months Ended December 26, 2015 and December 27, 2014	5
Condensed Consolidated Statements of Cash Flows for the Three Months Ended December 26, 2015 and December 27, 2014	6
Notes to Unaudited Interim Financial Statements	7
Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations	12
Item 3. Quantitative and Qualitative Disclosures About Market Risk	19
Item 4. Controls and Procedures	19
Part II – Other Information	
Item 6. Exhibits	19
Signatures	22



## Part I. FINANCIAL INFORMATION

## Item 1. FINANCIAL STATEMENTS

## INGLES MARKETS, INCORPORATED AND SUBSIDIARIES

## CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

	December 26, 2015	September 26, 2015
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 8,548,884	\$ 7,505,040
Receivables - net	80,613,279	66,284,163
Inventories	341,275,978	338,644,128
Other current assets	11,121,337	11,313,152
Total Current Assets	441,559,478	423,746,483
Property and Equipment – Net	1,226,718,716	1,211,458,393
Other Assets	19,730,986	19,623,349
Total Assets	\$ 1,688,009,180	\$ 1,654,828,225
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current Liabilities:		
Current portion of long-term debt	\$ 11,238,058	\$ 11,367,710
Accounts payable - trade	166,726,570	166,039,952
Accrued expenses and current portion of other long-term liabilities	53,892,007	74,552,234
Total Current Liabilities	231,856,635	251,959,896
Deferred Income Taxes	68,869,000	64,643,000
Long-Term Debt	913,513,109	874,685,817
Other Long-Term Liabilities	35,060,450	34,561,112
Total Liabilities	1,249,299,194	1,225,849,825
Stockholders' Equity		
Preferred stock, \$0.05 par value; 10,000,000 shares authorized; no shares issued	—	—
Common stocks:		
Class A, \$0.05 par value; 150,000,000 shares authorized; 13,942,826 shares issued and outstanding December 26, 2015; 13,924,651 shares issued and outstanding at September 26, 2015	697,142	696,233
Class B, convertible to Class A, \$0.05 par value; 100,000,000 shares authorized; 6,316,950 shares issued and outstanding December 26, 2015; 6,335,125 shares	315,847	316,756

Edgar Filing: INGLES MARKETS INC - Form 10-Q

issued and outstanding at September 26, 2015

Paid-in capital in excess of par value	12,311,249	12,311,249
Retained earnings	425,385,748	415,654,162
Total Stockholders' Equity	438,709,986	428,978,400
Total Liabilities and Stockholders' Equity	\$ 1,688,009,180	\$ 1,654,828,225

See notes to unaudited condensed consolidated financial statements.

3

---

## INGLES MARKETS, INCORPORATED AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

	Three Months Ended	
	December 26, 2015	December 27, 2014
Net sales	\$ 951,113,863	\$ 964,496,835
Cost of goods sold	725,474,531	740,104,278
Gross profit	225,639,332	224,392,557
Operating and administrative expenses	194,072,287	186,978,851
Gain from sale or disposal of assets	63,731	117,781
Income from operations	31,630,776	37,531,487
Other income, net	605,844	562,760
Interest expense	11,977,197	12,022,909
Income before income taxes	20,259,423	26,071,338
Income tax expense	7,280,000	11,033,000
Net income	\$ 12,979,423	\$ 15,038,338
Per share amounts:		
Class A Common Stock		
Basic earnings per common share	\$ 0.66	\$ 0.77
Diluted earnings per common share	\$ 0.64	\$ 0.74
Class B Common Stock		
Basic earnings per common share	\$ 0.60	\$ 0.70
Diluted earnings per common share	\$ 0.60	\$ 0.70
Cash dividends per common share		
Class A Common Stock	\$ 0.165	\$ 0.165
Class B Common Stock	\$ 0.150	\$ 0.150

See notes to unaudited condensed consolidated financial statements.



## INGLES MARKETS, INCORPORATED AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (UNAUDITED)

THREE MONTHS ENDED DECEMBER 26, 2015 AND DECEMBER 27, 2014

	Class A Common Stock		Class B Common Stock		Paid-in Capital in Excess of Par Value	Retained Earnings	Total
	Shares	Amount	Shares	Amount			
Balance, September 27, 2014	13,540,333	\$ 677,017	6,719,443	\$ 335,972	\$ 12,311,249	\$ 369,277,929	\$ 382,602,167
Net income	—	—	—	—	—	15,038,338	15,038,338
Cash dividends	—	—	—	—	—	(3,243,072)	(3,243,072)
Common stock conversions	13,100	655	(13,100)	(655)	—	—	—
Balance, December 27, 2014	13,553,433	\$ 677,672	6,706,343	\$ 335,317	\$ 12,311,249	\$ 381,073,195	\$ 394,397,433
Balance, September 26, 2015	13,924,651	\$ 696,233	6,335,125	\$ 316,756	\$ 12,311,249	\$ 415,654,162	\$ 428,978,400
Net income	—	—	—	—	—	12,979,423	12,979,423
Cash dividends	—	—	—	—	—	(3,247,837)	(3,247,837)
Common stock conversions	18,175	909	(18,175)	(909)	—	—	—
Balance, December 26, 2015	13,942,826	\$ 697,142	6,316,950	\$ 315,847	\$ 12,311,249	\$ 425,385,748	\$ 438,709,986

See notes to unaudited condensed consolidated financial statements.

5

---

## INGLES MARKETS, INCORPORATED AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	Three Months Ended	
	December 26, 2015	December 27, 2014
Cash Flows from Operating Activities:		
Net income	\$ 12,979,423	\$ 15,038,338
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization expense	25,976,526	25,298,752
Gain from sale or disposal of assets	(63,731)	(117,781)
Receipt of advance payments on purchases contracts	1,000,000	1,095,220
Recognition of advance payments on purchases contracts	(817,349)	(962,065)
Deferred income taxes	4,226,000	4,997,000
Changes in operating assets and liabilities:		
Receivables	(14,329,115)	(10,751,029)
Inventory	(2,631,850)	(8,797,151)
Other assets	84,177	(997,523)
Accounts payable and accrued expenses	(19,921,052)	(29,632,041)
Net Cash Provided (Used) by Operating Activities	6,503,029	(4,828,280)
Cash Flows from Investing Activities:		
Proceeds from sales of property and equipment	51,133	168,024
Capital expenditures	(40,639,588)	(27,573,589)
Net Cash Used by Investing Activities	(40,588,455)	(27,405,565)
Cash Flows from Financing Activities:		
Proceeds from short-term borrowings	240,823,511	233,849,691
Payments on short-term borrowings	(200,432,718)	(198,759,741)
Principal payments on long-term borrowings	(2,013,686)	(1,969,558)
Dividends paid	(3,247,837)	(3,243,072)
Net Cash Provided by Financing Activities	35,129,270	29,877,320
Net Increase (Decrease) in Cash and Cash Equivalents	1,043,844	(2,356,525)
Cash and cash equivalents at beginning of period	7,505,040	8,613,628
Cash and Cash Equivalents at End of Period	\$ 8,548,884	\$ 6,257,103

See notes to unaudited condensed consolidated financial statements.

INGLES MARKETS, INCORPORATED AND SUBSIDIARIES

NOTES TO UNAUDITED INTERIM FINANCIAL STATEMENTS

Three Months Ended December 26, 2015 and December 27, 2014

A. BASIS OF PREPARATION

In the opinion of management, the accompanying unaudited interim financial statements contain all adjustments necessary to present fairly the Company's financial position as of December 26, 2015, and the results of operations, changes in stockholders' equity and cash flows for the three months ended December 26, 2015 and December 27, 2014. The adjustments made are of a normal recurring nature. Certain information and footnote disclosures normally included in the annual financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission for Form 10-Q. It is suggested that these unaudited interim financial statements be read in conjunction with the audited financial statements and the notes thereto included in the Annual Report on Form 10-K for the year ended September 26, 2015, filed by the Company under the Securities Exchange Act of 1934 on December 10, 2015.

The results of operations for the three-month period ended December 26, 2015 are not necessarily indicative of the results to be expected for the full fiscal year.

B. NEW ACCOUNTING PRONOUNCEMENTS

In April 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update ASU 2015-03 "Simplifying the Presentation of Debt Issuance Costs" (ASU 2015-03). ASU 2015-03 changes the presentation of debt issuance costs in financial statements. Upon adoption of ASU 2015-03, debt issuance costs will be reported in the balance sheet as a direct deduction from the related debt liability rather than as an asset. The Company adopted ASU 2015-03 retroactively during the quarter ended December 26, 2015. As a result, \$9.0 million and \$9.3 million of debt issuance costs were recorded as a reduction of total debt at December 26, 2015 and September 26, 2015, respectively.

In November 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update ASU 2015-17 "Balance Sheet Classification of Deferred Taxes" (ASU 2015-17). ASU 2015-17 requires entities to present deferred tax assets and deferred tax liabilities as noncurrent in a classified balance sheet. ASU 2015-07 simplifies current guidance, which requires entities to separately present deferred tax assets and deferred tax liabilities as current and noncurrent in a classified balance sheet. The Company adopted ASU 2015-17 retroactively during the quarter ended December 26, 2015. As a result, \$7.3 million of deferred tax assets were recorded as a reduction of the caption "Deferred Income Taxes" in the Condensed Consolidated Balance Sheets at December 26, 2015 and September 26,

2015.

#### C. ALLOWANCE FOR DOUBTFUL ACCOUNTS

Receivables are presented net of an allowance for doubtful accounts of \$400,000 at December 26, 2015 and September 26, 2015, respectively.

#### D. INCOME TAXES

The Company's effective tax rate differs from the federal statutory rate primarily as a result of state income taxes and tax credits.

The Company had approximately \$3.0 million of refundable income taxes included in the caption "Other current assets" in the Condensed Consolidated Balance Sheets at December 26, 2015.

The Company has unrecognized tax benefits and could incur interest and penalties related to uncertain tax positions.. These amounts are insignificant and are not expected to significantly increase or decrease within the next twelve months.

On September 13, 2013, the IRS released final tangible property regulations under Sections 162(a) and 263(a) of the Internal Revenue Code regarding the deduction and capitalization of expenditures related to tangible property as well as dispositions of tangible property. These regulations were effective for the Company's fiscal year ending September 26, 2015 and did not have a material impact on the Company's consolidated results of operations, cash flows or financial position for the fiscal quarters ended December 26, 2015 and December 27, 2014.

## E. ACCRUED EXPENSES AND CURRENT PORTION OF OTHER LONG-TERM LIABILITIES

Accrued expenses and current portion of other long-term liabilities consist of the following:

	December 26, 2015	September 26, 2015
Property, payroll and other taxes payable	\$ 12,276,842	\$ 17,882,565
Salaries, wages and bonuses payable	21,593,323	26,336,530
Self-insurance liabilities	14,419,179	14,724,793
Interest payable	2,600,206	12,623,691
Other	3,002,457	2,984,655
	\$ 53,892,007	\$ 74,552,234

Self-insurance liabilities are established for general liability claims, workers' compensation and employee group medical and dental benefits based on claims filed and estimates of claims incurred but not reported. The Company is insured for covered costs in excess of \$750,000 per occurrence for workers' compensation, \$500,000 for general liability and \$325,000 per covered person for medical care benefits for a policy year. At December 26, 2015 the Company's self-insurance reserves totaled \$36.0 million. Of this amount, \$14.4 million is accounted for as a current liability and \$21.6 million as a long-term liability, which is inclusive of \$5.2 million of expected self-insurance recoveries from excess cost insurance or other sources that are recorded as a receivable at December 26, 2015. Employee insurance expense, including workers' compensation and medical care benefits, net of employee contributions, totaled \$9.2 million and \$7.8 million for the three-month periods ended December 26, 2015 and December 27, 2014, respectively.

## F. LONG-TERM DEBT

In June 2013, the Company issued \$700.0 million aggregate principal amount of senior notes due in 2023 (the "Notes") in a private placement. The Notes bear an interest rate of 5.750% per annum and were issued at par.

The Company filed a registration statement with the Securities and Exchange Commission and completed the exchange of private placement notes with registered notes.

The Company may redeem all or a portion of the Notes at any time on or after June 15, 2018 at the following redemption prices (expressed as percentages of the principal amount), if redeemed during the 12-month period beginning June 15 of the years indicated below:

Year	
2018	102.875%
2019	101.917%
2020	100.958%
2021 and thereafter	100.000%

In connection with the offering of the Notes, the Company extended the maturity date of its \$175.0 million line of credit (the "Line") from December 29, 2015 to June 12, 2018 and modified certain interest rate options and covenants. At December 26, 2015, the Company had \$40.9 million of borrowings outstanding under the Line.

The Line provides the Company with various interest rate options based on the prime rate, the Federal Funds Rate, or the London Interbank Offering Rate ("LIBOR"). The Line allows the Company to issue up to \$30.0 million in unused letters of credit, of which \$10.1 million of unused letters of credit were issued at December 26, 2015. The Company is not required to maintain compensating balances in connection with the Line.

On December 29, 2010, the Company completed the funding of \$99.7 million of bonds for construction of new warehouse and distribution space adjacent to its existing space in Buncombe County, North Carolina (the "Project"). The final maturity date of the bonds is January 1, 2036.

The bonds were issued by the Buncombe County Industrial Facilities and Pollution Control Financing Authority and were purchased by certain financial institutions. Under a Continuing Covenant and Collateral Agency Agreement (the "Covenant Agreement") between the financial institutions and the Company, the financial institutions would hold the bonds until January 2, 2018, subject to certain events. Mandatory redemption of the bonds by the Company in the annual amount of \$4,530,000 began on January 1, 2014.

In connection with the offering of the Notes, the Company extended the maturity date of the Covenant Agreement from January 2, 2018 to June 30, 2021 and modified certain interest rate options and covenants. The Company may redeem the bonds without penalty or premium at any time prior to June 30, 2021.

Interest earned by bondholders on the bonds is exempt from Federal and North Carolina income taxation. The interest rate on the bonds is equal to one month LIBOR (adjusted monthly) plus a credit spread, adjusted to reflect the income tax exemption.

The Company's obligation to repay the Bonds is collateralized by the Project. Additional collateral was required in order to meet certain loan to value criteria in the Covenant Agreement. The Covenant Agreement incorporates substantially all financial covenants included in the line of credit.

The Notes, the bonds and the Line contain provisions that under certain circumstances would permit lending institutions to terminate or withdraw their respective extensions of credit to the Company. Included among the triggering factors permitting the termination or withdrawal of the Line to the Company are certain events of default, including both monetary and non-monetary defaults, the initiation of bankruptcy or insolvency proceedings, and the failure of the Company to meet certain financial covenants designated in its respective loan documents. The Company was in compliance with all financial covenants at December 26, 2015.

The Company's long-term debt agreements generally have cross-default provisions which could result in the acceleration of payments due under the Company's line of credit, bonds and Notes indenture in the event of default under any one instrument.

#### G. DIVIDENDS

The Company paid cash dividends of \$0.165 for each share of Class A Common Stock and \$0.15 for each share of Class B Common Stock on October 22, 2015 to stockholders of record on October 8, 2015.

For additional information regarding the dividend rights of the Class A Common Stock and Class B Common Stock, please see Note 8, "Stockholders' Equity" to the Consolidated Financial Statements of the Annual Report on Form 10-K filed by the Company under the Securities Exchange Act of 1934 on December 10, 2015.

#### H. EARNINGS PER COMMON SHARE

The Company has two classes of common stock: Class A which is publicly traded, and Class B, which has no public market. The Class B Common Stock has restrictions on transfer; however, each share is convertible into one share of Class A Common Stock at any time. Each share of Class A Common Stock has one vote per share and each share of



Class B Common Stock has ten votes per share. Each share of Class A Common Stock is entitled to receive cash dividends equal to 110% of any cash dividend paid on Class B Common Stock.

The Company calculates earnings per share using the two-class method in accordance with FASB ASC Topic 260.

The two-class method of computing basic earnings per share for each period reflects the cash dividends declared per share for each class of stock, plus allocated undistributed earnings per share computed using the participation percentage which reflects the dividend rights of each class of stock. Diluted earnings per share is calculated assuming the conversion of all shares of Class B Common Stock to shares of Class A Common Stock on a share-for-share basis. The tables below reconcile the numerators and denominators of basic and diluted earnings per share for current and prior periods.

	Three Months Ended December 26, 2015		Three Months Ended December 27, 2014	
	Class A	Class B	Class A	Class B
Numerator: Allocated net income				
Net income allocated, basic	\$ 9,182,887	\$ 3,796,536	\$ 10,363,890	\$ 4,674,448
Conversion of Class B to Class A shares	3,796,536	—	4,674,448	—
Net income allocated, diluted	\$ 12,979,423	\$ 3,796,536	\$ 15,038,338	\$ 4,674,448
Denominator: Weighted average shares outstanding				
Weighted average shares outstanding, basic	13,926,923	6,332,853	13,542,924	6,716,852
Conversion of Class B to Class A shares	6,332,853	—	6,716,852	—
Weighted average shares outstanding, diluted	20,259,776	6,332,853	20,259,776	6,716,852
Earnings per share				
Basic	\$ 0.66	\$ 0.60	\$ 0.77	\$ 0.70
Diluted	\$ 0.64	\$ 0.60	\$ 0.74	\$ 0.70

I. SEGMENT INFORMATION

The Company operates one primary business segment, retail grocery sales. "Other" includes our remaining operations - fluid dairy and shopping center rentals. Information about the Company's operations by lines of business (amounts in thousands) is as follows:

Three  
Months  
Ended