ROCKY BRANDS, INC.
Form 10-Q
May 01, 2008

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2008

OR

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 number: 0-21026

ROCKY BRANDS, INC.

(Exact name of registrant as specified in its charter)

Ohio	**31-1364046**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

39 E. Canal Street, Nelsonville, Ohio 45764

(Address of Principal Executive Offices, Including Zip Code)

(740) 753-1951

(Registrant s Telephone Number, Including Area Code)

Not Applicable

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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, 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 o	Accelerated filer þ	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company 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

As of April 25, 2008, 5,508,398 shares of Rocky Brands, Inc. common stock, no par value, were outstanding.

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PART I FINANCIAL INFORMATION
ITEM 1 FINANCIAL STATEMENTS

ROCKY BRANDS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

	March 31, 2008 (Unaudited)	December 31, 2007	March 31, 2007 (Unaudited)
ASSETS:			
CURRENT ASSETS:			
Cash and cash equivalents	$ 4,407,629	$ 6,537,884	$ 1,776,893
Trade receivables net	56,189,187	65,931,092	58,953,715
Other receivables	947,296	674,707	1,222,207
Inventories	79,841,429	75,403,664	71,831,189
Deferred income taxes	1,952,536	1,952,536	3,902,775
Income tax receivable	607,910	719,945	3,079,485
Prepaid expenses	3,049,971	2,226,920	1,873,910
Total current assets	146,995,958	153,446,748	142,640,174
FIXED ASSETS net	23,943,273	24,484,050	23,897,559
DEFERRED PENSION ASSET			26,998
IDENTIFIED INTANGIBLES	36,361,267	36,509,690	36,966,851
GOODWILL			24,874,368
OTHER ASSETS	2,099,762	2,284,039	2,416,357
TOTAL ASSETS	$ 209,400,260	$ 216,724,527	$ 230,822,307
LIABILITIES AND SHAREHOLDERS EQUITY:			
CURRENT LIABILITIES:			
Accounts payable	$ 12,801,456	$ 11,908,902	$ 12,782,486
Current maturities long term debt	331,411	324,648	7,294,702
Accrued expenses:			
Salaries and wages	575,071	751,134	523,406
Co-op advertising	229,706	840,818	163,510
Interest	1,636,196	487,446	1,597,843
Taxes other	807,557	516,038	510,935
Commissions	454,462	717,564	782,244
Other	2,964,539	2,624,121	1,947,349
Total current liabilities	19,800,398	18,170,671	25,602,475
LONG TERM DEBT less current maturities	93,768,649	103,220,384	82,567,824
DEFERRED INCOME TAXES	12,951,828	13,247,953	17,009,025
DEFERRED PENSION LIABILITY	970,507	125,724	
DEFERRED LIABILITIES	246,699	235,204	312,542
TOTAL LIABILITIES	127,738,081	134,999,936	125,491,866
COMMITMENTS AND CONTINGENCIES			
SHAREHOLDERS EQUITY:			
	54,144,545	53,997,960	53,649,754

Common stock, no par value; 25,000,000 shares authorized; issued and outstanding March 31, 2008 - 5,508,278; December 31, 2007 - 5,488,293; March 31, 2007 - 5,466,543			
Accumulated other comprehensive loss	(1,538,049)	(1,051,232)	(967,609)
Retained earnings	29,055,683	28,777,863	52,648,296
Total shareholders equity	81,662,179	81,724,591	105,330,441
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	$ 209,400,260	$ 216,724,527	$ 230,822,307

See notes to the interim unaudited condensed consolidated financial statements.

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ROCKY BRANDS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	Three Months Ended March 31,	
	2008	2007
NET SALES	$ 60,484,716	$ 61,657,024
COST OF GOODS SOLD	34,535,051	35,576,338
GROSS MARGIN	25,949,665	26,080,686
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	23,061,487	22,322,941
INCOME FROM OPERATIONS	2,888,178	3,757,745
OTHER INCOME AND (EXPENSES):		
Interest expense, net	(2,406,671)	(2,498,845)
Other net	(18,592)	(42,995)
Total other net	(2,425,263)	(2,541,840)
INCOME BEFORE INCOME TAXES	462,915	1,215,905
INCOME TAX EXPENSE	162,000	450,000
NET INCOME	$ 300,915	$ 765,905
NET INCOME PER SHARE		
Basic	$ 0.05	$ 0.14
Diluted	$ 0.05	$ 0.14
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING		
Basic	5,507,839	5,457,556
Diluted	5,526,479	5,594,930

See notes to the interim unaudited condensed consolidated financial statements.

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ROCKY BRANDS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	Three Months Ended March 30,	
	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 300,915	$ 765,905
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	1,495,827	1,371,353
Deferred compensation and other	50,241	(43,899)
(Gain) Loss on disposal of fixed assets	(38,334)	2,080
Stock compensation expense	146,584	170,443
Change in assets and liabilities		
Receivables	9,469,316	6,243,102
Inventories	(4,437,765)	6,117,787
Other current assets	(711,016)	260,717
Other assets	184,278	380,419
Accounts payable	914,624	2,598,945
Accrued and other liabilities	730,410	1,329,001
Net cash provided by operating activities	8,105,080	19,195,853
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of fixed assets	(810,887)	(734,363)
Investment in trademarks and patents	(17,937)	(27,265)
Proceeds from sale of fixed assets	38,461	
Net cash used in investing activities	(790,363)	(761,628)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from revolving credit facility	62,497,654	54,594,784
Repayments of revolving credit facility	(71,863,957)	(73,380,198)
Repayments of long-term debt	(78,669)	(1,843,641)
Proceeds from exercise of stock options		240,470
Net cash used in financing activities	(9,444,972)	(20,388,585)
DECREASE IN CASH AND CASH EQUIVALENTS	(2,130,255)	(1,954,360)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	6,537,884	3,731,253

CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 4,407,629	$ 1,776,893

See notes to the interim unaudited condensed consolidated financial statements.

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ROCKY BRANDS, INC.
AND SUBSIDIARIES

NOTES TO THE INTERIM UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE-MONTH PERIOD ENDED MARCH 31, 2008 AND 2007

1. INTERIM FINANCIAL REPORTING

In the opinion of management, the accompanying interim unaudited condensed consolidated financial statements reflect all adjustments that are necessary for a fair presentation of the financial results. All such adjustments reflected in the unaudited interim consolidated financial statements are considered to be of a normal and recurring nature. The results of the operations for the three-month periods ended March 31, 2008 and 2007 are not necessarily indicative of the results to be expected for the whole year. Accordingly, these condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto contained in our Annual Report on Form 10-K for the year ended December 31, 2007.

The components of total comprehensive income are shown below:

	(Unaudited) Three Months Ended March 31, 2008	(Unaudited) Three Months Ended March 31, 2007
Net income	$ 300,915	$ 765,905
Other comprehensive income:		
Amortization of unrecognized transition obligation, service cost and net loss	40,032	25,573
Total comprehensive income	$ 340,947	$ 791,478

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2. INVENTORIES

Inventories are comprised of the following:

	March 31, 2008 (Unaudited)	December 31, 2007	March 31, 2007 (Unaudited)
Raw materials	$ 7,462,809	$ 6,086,118	$ 6,603,390
Work-in-process	741,731	144,171	995,124
Finished goods	71,781,889	69,301,375	64,532,675
Reserve for obsolescence or lower of cost or market	(145,000)	(128,000)	(300,000)
Total	$ 79,841,429	$ 75,403,664	$ 71,831,189

In 2006, the U.S. Military cancelled a contract for convenience. We had previously purchased raw materials exclusively to fulfill this contract. In March 2007, we received a partial settlement of the contract and finalized the ultimate settlement of the contract in June 2007. As a result of this settlement and other third-party sales, the value of the raw material inventory purchased in 2006 was realized. In addition, the settlement provided for a reimbursement of expenses incurred in prior periods. This reimbursement is recognized as a reduction of cost of goods sold of approximately $0.7 million the first quarter of 2007.

3. SUPPLEMENTAL CASH FLOW INFORMATION

Supplemental cash information including, cash paid for interest and Federal, state and local income taxes, net of refunds, was as follows:

	Three Months Ended March 31, 2008	Three Months Ended March 31, 2007
Interest	$ 1,117,351	$ 1,033,000
Federal, state and local income taxes	$ 49,965	$ 97,000
Fixed asset purchases in accounts payable	$ 34,096	$ 21,250

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4. PER SHARE INFORMATION

Basic earnings per share (EPS) is computed by dividing net income applicable to common shareholders by the weighted average number of common shares outstanding during each period. The diluted earnings per share computation includes common share equivalents, when dilutive. There are no adjustments to net income necessary in the calculation of basic and diluted earnings per share.

A reconciliation of the shares used in the basic and diluted income per common share computation for the three months ended March 31, 2008 and 2007 is as follows:

	Three Months Ended March 31,	
	2008	2007
Weighted average shares outstanding	5,507,839	5,457,556
Diluted stock options	18,640	137,374
Diluted weighted average shares outstanding	5,526,479	5,594,930
Anti-diluted weighted average shares outstanding	290,464	264,125

5. RECENT FINANCIAL ACCOUNTING STANDARDS

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. In February 2008, the FASB issued *FASB Staff Position No. FAS 157-2, Effective Date of FASB Statement No. 157* (FSP FAS 157-2). FSP FAS 157-2 defers implementation of SFAS 157 for certain non-financial assets and non-financial liabilities. SFAS 157 is effective for financial assets and liabilities in fiscal years beginning after November 15, 2007 and for non-financial assets and liabilities in fiscal years beginning after March 15, 2008. We have evaluated the impact of the provisions applicable to our financial assets and liabilities and have determined that there will not be a material impact on our consolidated financial statements. The aspects that have been deferred by FSP FAS 157-2 pertaining to non-financial assets and non-financial liabilities will be effective for us beginning January 1, 2009. We are currently reviewing SFAS 157 and FSP FAS 157-2 to determine the impact and materiality of their adoption on our consolidated financial statements.

In September 2006, the FASB issued SFAS No. 158, *Employers Accounting for Defined Benefits Pension and Other Postretirement Plans, an Amendment of FASB Statements 87, 88, 106, and 132(R)* (SFAS 158). SFAS 158, requires an employer to recognize in its statement of financial position the funded status of its defined benefit plans and to recognize as a component of other comprehensive income, net of tax, any unrecognized transition obligations and assets, the actuarial gains and losses and prior service costs and credits that arise during the period. The recognition provisions of SFAS 158 were effective for fiscal years ending after December 15, 2006. The adoption of SFAS 158 as of December 31, 2006 resulted in a write-down of our pension asset by $1.6 million, increased accumulated other comprehensive loss by $1.0 million, and decreased deferred income tax liabilities by $0.6 million. In addition, SFAS 158 requires a fiscal year end measurement of plan assets and benefit obligations, eliminating the use of earlier measurement dates previously permissible. However, the new measurement date requirement is effective and we have changed our measurement date to December 31st.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of statement No. 115* (SFAS 159). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The standard also establishes presentation and disclosure requirements designed to facilitate comparison between entities that choose different measurement attributes for similar types of assets and liabilities. SFAS 159 is effective for annual periods in fiscal years beginning after November 15, 2007. If the fair value option is elected, the effect of the first re-measurement to fair value is reported as a cumulative effect adjustment to the opening balance of retained earnings. In the event we elect the fair value option promulgated by this standard, the valuations of certain assets and liabilities may be impacted. The statement is applied prospectively upon adoption. We have evaluated the impact of the provisions of SFAS 159 and have determined that there will not be a material impact on our consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141R, *Business Combinations* (SFAS 141R). SFAS 141R replaces SFAS 141, *Business Combinations.* The objective of SFAS 141R is to improve the relevance, representational faithfulness and comparability of the information that a reporting entity provides in its financial reports about a business combination and its effects. SFAS 141R establishes principles and requirements for how the acquirer: a) recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree; b) recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase option; and c) determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. SFAS 141R applies prospectively to business combinations for which the acquisition date is on of after the beginning of the first annual reporting period beginning on or after December 15, 2008. Early adoption of SFAS 141R is prohibited. We do not anticipate the adoption of SFAS 141R will have a material impact on our financial statements.

In December 2007, the FASB issued SFAS No, 160, *Non-controlling Interests in Consolidated Financial Statements, an amendment of ARB No, 51* (SFAS 160). The objective of SFAS 160 is to improve the relevance, comparability, and transparency of the financial information that a reporting entity provides in its consolidated financial statements by establishing certain accounting and reporting standards that address: the ownership interests in subsidiaries held by parties other than the parent; the amount of net income attributable to the parent and non-controlling interest; changes in the parent s ownership interest; and any retained non-controlling equity investment in a deconsolidated subsidiary. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. Early adoption of SFAS 160 is prohibited. We do not anticipate the adoption of

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SFAS 160 will have a material impact on our financial statements.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB No. 133* (SFAS 161). SFAS 161 intends to improve financial reporting about derivative instruments and hedging activities by requiring enhanced disclosures to enable investors to better understand their effects on an entity s financial position, financial performance and cash flows. SFAS 161 also requires disclosure about an entity s strategy and objectives for using derivatives, the fair values of derivative instruments and their related gains and losses. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early application encouraged. The statement encourages, but does not require, comparative disclosures for earlier periods at initial adoption. We are currently evaluating the impact of adopting SFAS 161 and do not anticipate that its adoption will have a material impact on our consolidated financial statements.

6. INCOME TAXES

We file income tax returns in the U.S. Federal jurisdiction and various state and foreign jurisdictions. An examination of our 2004 Federal income tax return resulted in an immaterial adjustment. The examination of the 2003 Federal income tax return resulted in no changes. We are no longer subject to U.S. Federal tax examinations for years before 2003. State jurisdictions that remain subject to examination range from 2003 to 2006. Foreign jurisdiction (Canada and Puerto Rico) tax returns that remain subject to examination range from 2001 to 2006. We do not believe there will be any material changes in our unrecognized tax positions over the next 12 months.

Our policy is to recognize interest and penalties accrued on any unrecognized tax benefits as a component of income tax expense. As of the date of adoption of FIN 48, accrued interest or penalties were not material, and no such expenses were recognized during the quarter.

We provided for income taxes at estimated effective tax rates of 35% and 37% for the three-month periods ended March 31, 2008 and 2007, respectively.

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7. INTANGIBLE ASSETS

A schedule of intangible assets is as follows:

March 31, 2008 (unaudited)	Gross Amount	Accumulated Amortization	Carrying Amount
Trademarks:			
Wholesale	$ 28,278,596	$ 107,814	$ 28,170,782
Retail	6,900,000		6,900,000
Patents	2,287,988	1,347,503	940,485
Customer relationships	1,000,000	650,000	350,000
Total Identified Intangibles	$ 38,466,584	$ 2,105,317	$ 36,361,267

December 31, 2007	Gross Amount	Accumulated Amortization	Carrying Amount
Trademarks:			
Wholesale	$ 28,272,514	$ 86,251	$ 28,186,263
Retail	6,900,000		6,900,000
Patents	2,276,132	1,252,705	1,023,427
Customer relationships	1,000,000	600,000	400,000
Total Identified Intangibles	$ 38,448,646	$ 1,938,956	$ 36,509,690

March 31, 2007 (unaudited)	Gross Amount	Accumulated Amortization	Carrying Amount
Trademarks:			
Wholesale	$ 28,250,046	$ 21,563	$ 28,228,483
Retail	6,900,000		6,900,000
Patents	2,257,570	969,202	1,288,368
Customer relationships	1,000,000	450,000	550,000
Total Identified Intangibles	$ 38,407,616	$ 1,440,765	$ 36,966,851

Amortization expense for intangible assets was $166,361 and $165,705 for the three months ended March 31, 2008 and 2007, respectively. The weighted average amortization period for patents is six years and for customer relationships is five years.

Estimate of Aggregate Amortization Expense for the years ending December 31,:

2009	$665,446
2010	125,363
2011	123,983
2012	123,983
2013	123,983

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8. CAPITAL STOCK

On May 11, 2004, our shareholders approved the 2004 Stock Incentive Plan. The Plan includes 750,000 of our common shares that may be granted for stock options and restricted stock awards. As of March 31, 2008, we were authorized to issue approximately 406,420 shares under our existing plans.

The plan generally provides for grants with the exercise price equal to fair value on the date of grant, graduated vesting periods of up to five years, and lives not exceeding ten years. The following summarizes stock option transactions from January 1, 2008 through March 31, 2008:

	Shares	Weighted Average Exercise Price
Options outstanding at January 1, 2008	472,551	$15.37
Issued		$
Exercised		$
Forfeited		