ALBANY INTERNATIONAL CORP /DE/
Form 10-Q
August 09, 2011
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: June 30, 2011

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: 1-10026

ALBANY INTERNATIONAL CORP.
(Exact name of registrant as specified in its charter)

Delaware	14-0462060
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
216 Airport Drive, Rochester, New Hampshire	03867
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code 518-445-2200

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.

Large accelerated filer	[ ]	Accelerated filer	[√]
Non-accelerated filer	[ ]	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 [√]

The registrant had 28.0 million shares of Class A Common Stock and 3.2 million shares of Class B Common Stock outstanding as of June 30, 2011.

ALBANY INTERNATIONAL CORP.

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ALBANY INTERNATIONAL CORP.
CONSOLIDATED STATEMENTS OF INCOME
(in thousands, except per share data)
(unaudited)

Three Months Ended June 30, 2011	Three Months Ended June 30, 2010		Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
$244,015	$227,450	Net sales	$495,865	$441,323
149,115	141,615	Cost of goods sold	295,972	278,259
94,900	85,835	Gross profit	199,893	163,064
58,359	46,482	Selling, general, and administrative expenses	116,124	99,392
15,367	14,884	Technical, product engineering, and research expenses	30,502	28,050
2,092	689	Restructuring and other, net	2,278	2,081
19,082	23,780	Operating income	50,989	33,541
4,786	3,882	Interest expense, net	9,562	7,707
55	(2,991)	Other expense/(income), net	4,924	(5,272)
14,241	22,889	Income before income taxes	36,503	31,106
5,359	15,102	Income tax expense	10,668	17,729
8,882	7,787	Income before equity in (losses)/earnings of associated companies	25,835	13,377
(120)	90	Equity in (losses)/earnings of associated companies	(340)	98
$8,762	$7,877	Net income	$25,495	$13,475
		Net income per share:		
$0.28	$0.25	Basic	$0.82	$0.43
$0.28	$0.25	Diluted	$0.81	$0.43
		Shares used in computing earnings per share:		
31,263	31,058	Basic	31,243	31,001
31,489	31,161	Diluted	31,455	31,105
$0.13	$0.12	Dividends per share	$0.25	$0.24

The accompanying notes are an integral part of the consolidated financial statements

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ALBANY INTERNATIONAL CORP.
CONSOLIDATED BALANCE SHEETS
(in thousands, except share and per share data)
(unaudited)

	June 30, 2011	December 31, 2010
ASSETS		
Cash and cash equivalents	$157,046	$122,301
Accounts receivable, net	178,788	176,716
Inventories	179,729	156,171
Income taxes receivable and deferred	43,448	39,721
Prepaid expenses and other current assets	14,619	11,883
Total current assets	573,630	506,792
Property, plant and equipment, net	484,301	488,121
Investments in associated companies	3,254	2,926
Intangibles	3,351	4,182
Goodwill	122,542	115,616
Deferred taxes	142,638	141,701
Other assets	18,344	18,955
Total assets	$1,348,060	$1,278,293
LIABILITIES AND SHAREHOLDERS' EQUITY		
Notes and loans payable	$1,246	$1,587
Accounts payable	51,895	44,294
Accrued liabilities	110,864	110,292
Current maturities of long-term debt	12	12
Income taxes payable and deferred	14,960	9,670
Total current liabilities	178,977	165,855
Long-term debt	417,012	423,647
Other noncurrent liabilities	192,718	190,493
Deferred taxes and other credits	73,185	72,038
Total liabilities	861,892	852,033
Commitments and Contingencies	-	-
SHAREHOLDERS' EQUITY		
Preferred stock, par value $5.00 per share; authorized 2,000,000 shares; none issued	-	-

Class A Common Stock, par value $.001 per share; authorized 100,000,000 shares; issued 36,515,942 in 2011 and 36,442,209 in 2010	37	36
Class B Common Stock, par value $.001 per share; authorized 25,000,000 shares; issued and outstanding 3,236,098 in 2011 and 2010	3	3
Additional paid in capital	389,393	387,876
Retained earnings	420,729	403,048
Accumulated items of other comprehensive income:		
Translation adjustments	33,830	(6,041)
Pension and post retirement liability adjustments	(98,703)	(100,355)
Derivative valuation adjustment	(1,201)	(276)
Treasury stock (Class A), at cost 8,479,487 shares in 2011 and 8,484,528 shares in 2010	(257,920)	(258,031)
Total shareholders' equity	486,168	426,260
Total liabilities and shareholders' equity	$1,348,060	$1,278,293

The accompanying notes are an integral part of the consolidated financial statements

ALBANY INTERNATIONAL CORP.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(unaudited)

Three Months Ended June 30, 2011	Three Months Ended June 30, 2010		Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
		OPERATING ACTIVITIES		
$8,762	$7,877	Net income	$25,495	$13,475
		Adjustments to reconcile net income to net cash provided by operating activities:		
120	(90)	Equity in losses/(earnings) of associated companies	340	(98)
14,393	13,309	Depreciation	28,526	27,250
2,312	2,276	Amortization	4,489	4,230
181	189	Noncash interest expense	377	377
2,189	9,709	Provision for deferred income taxes, other credits and long-term liabilities	(24)	11,215
23	1,626	Provision for write-off of property, plant and equipment	64	3,093
(594)	-	Gain on disposition of assets	(1,022)	-
-	847	Decrease in cash surrender value of life insurance	-	-
(21)	-	Excess tax benefit of options exercised	(35)	-
950	2,054	Compensation and benefits paid or payable in Class A Common Stock	1,290	3,009
		Changes in operating assets and liabilities, net of business acquisitions and divestitures:		
5,049	(8,740)	Accounts receivable	6,905	(344)
(8,940)	9,748	Inventories	(17,312)	12,018
797	739	Prepaid expenses and other current assets	(2,473)	(2,030)
1,654	(2,369)	Accounts payable	3,902	(4,444)
1,343	3,429	Accrued liabilities	(4,090)	(8,693)
1,161	1,758	Income taxes payable	4,859	321
1,371	1,560	Other, net	507	1,443
30,750	43,922	Net cash provided by operating activities	51,798	60,822
		INVESTING ACTIVITIES		
(8,975)	(7,094)	Purchases of property, plant and equipment	(13,894)	(13,915)
(705)	(873)	Purchased software	(1,752)	(1,946)
1,159	-	Proceeds from sale of assets	2,860	-
-	-	Acquisitions, net of cash acquired	-	(1,902)
-	49,302	Cash received from life insurance policy terminations	-	49,302

(8,521)	41,335	Net cash (used in)/provided by investing activities	(12,786)	31,539
		FINANCING ACTIVITIES		
4	-	Proceeds from borrowings	644	6,152
(980)	(69,738)	Principal payments on debt	(7,997)	(69,755)
192	49	Proceeds from options exercised	301	136
21	-	Excess tax benefit of options exercised	35	-
(3,750)	(3,714)	Dividends paid	(7,494)	(7,419)
(4,513)	(73,403)	Net cash (used in) financing activities	(14,511)	(70,886)
1,812	(10,939)	Effect of exchange rate changes on cash and cash equivalents	10,244	(16,268)
19,528	915	Increase in cash and cash equivalents	34,745	5,207
137,518	101,758	Cash and cash equivalents at beginning of period	122,301	97,466
$157,046	$102,673	Cash and cash equivalents at end of period	$157,046	$102,673

The accompanying notes are an integral part of the consolidated financial statements

ALBANY INTERNATIONAL CORP.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. Basis of Presentation

In our opinion, the accompanying unaudited consolidated financial statements contain all adjustments, consisting of only normal, recurring adjustments, necessary for a fair presentation of results for such periods. The results for any interim period are not necessarily indicative of results for the full year. The preparation of financial statements for interim periods does not require all of the disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted. These consolidated financial statements should be read in conjunction with our Annual Report on Form 10-K as filed with the SEC for the year ended December 31, 2010.

In the first quarter of 2011, we modified our business segment reporting by reclassifying our Fiber Preparation business from the Engineered Fabrics segment to the Paper Machine Clothing segment. The change was made to better align our organizational structure with the customers that purchase these products. Prior year data has been modified to conform to the current year presentation. On April 29, 2011 we filed a current report on Form 8-K with reclassified segment data for quarterly periods in 2010, as well as annual data for 2010 and 2009.

In the first quarter of 2011, we adopted an accounting pronouncement related to revenue recognition principles for contracts with multiple revenue elements. This change, which affects the Albany Door Systems segment, accelerates revenue recognition associated with contracts that include both the sale of a door and installation services. We determine the consideration allocated to each revenue element at the inception of the arrangement, based on the relative fair values of the goods and services provided under the contract. The change was applied on a prospective basis, resulting in a one-time acceleration of net sales without the offsetting effect of applying the change to previous periods. As a result, we recognized in 2011 additional net sales and operating income, as follows:

(in thousands)	Three Months Ended June 30, 2011	Six Months Ended June 30, 2011
Net sales	($665)	$1,832
Operating income	(9)	953

The effect of this change on any future quarterly period could vary significantly due to timing, or the number and value of contracts that include both the sale of a door and installation services. Normally, installation is completed within a few months after the door is delivered.

2. Reportable Segment Data

The following table shows data by reportable segment, reconciled to consolidated totals included in the financial statements:

(in thousands)	Three Months Ended June 30, **2011**	2010	Six Months Ended June 30, **2011**	2010
Net Sales				
Paper Machine Clothing	**$158,577**	$153,662	**$326,473**	$300,399
Albany Door Systems	**45,393**	33,792	**90,521**	67,547
Engineered Fabrics	**20,600**	21,032	**41,186**	40,144
Engineered Composites	**10,504**	10,870	**21,976**	19,511
PrimaLoft® Products	**8,941**	8,094	**15,709**	13,722
Consolidated total	**$244,015**	$227,450	**$495,865**	$441,323
Operating income/(loss)				
Paper Machine Clothing	**$34,909**	$38,575	**$81,139**	$66,236
Albany Door Systems	**4,053**	2,339	**9,424**	5,223
Engineered Fabrics	**2,800**	3,835	**6,841**	5,492
Engineered Composites	**(1,144)**	(1,989)	**(2,187)**	(4,218)
PrimaLoft® Products	**3,165**	2,926	**5,076**	4,995
Research expense	**(7,212)**	(7,132)	**(14,377)**	(12,943)
Unallocated expenses	**(17,489)**	(14,774)	**(34,927)**	(31,244)
Operating income before reconciling items	**19,082**	23,780	**50,989**	33,541
Reconciling items:				
Interest expense, net	**4,786**	3,882	**9,562**	7,707
Other expense/(income), net	**55**	(2,991)	**4,924**	(5,272)
Income before income taxes	**$14,241**	$22,889	**$36,503**	$31,106

The table below presents restructuring costs by reportable segment for the three and six month periods ended June 30, 2011 and 2010:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in thousands)	**2011**	2010	**2011**	2010
Restructuring expense				
Paper Machine Clothing	**$448**	$676	**$481**	$2,962
Albany Door Systems	**361**	446	**513**	474
Engineered Fabrics	**124**	607	**124**	607
Engineered Composites	**44**	-	**57**	-
Unallocated	**1,115**	(1,040)	**1,103**	(1,962)
Consolidated total	**$2,092**	$689	**$2,278**	$2,081

The 2011 expense was principally due to organizational changes associated with the substantial completion of the SAP conversion project. The expense in 2010 was partially reduced by other post retirement curtailment gains, which was included in the Unallocated reportable segment.

There were no material changes in the total assets of reportable segments during this period.

3. Pensions and Other Benefits

We sponsor defined benefit pension plans in various countries. The amount of contributions to the plans is based on several factors including the funding rules in each country. Employer contributions of $22.1 million in 2010 included $13.2 million transferred into pension trusts, plus $8.9 million for benefits paid directly to participants. We expect 2011 contributions to be approximately $16.0 million, including $12.3 million to be transferred to pension trusts, plus $3.7 million for benefits paid directly to participants. We also provide certain medical, dental and life insurance benefits (Other Postretirement Benefits) for retired United States employees that meet program qualifications. We currently fund this plan as claims are paid.

The components of net periodic benefit cost for the six months ended June 30, 2011 and 2010 are, as follows:

(in thousands)	Pension Plans **2011**	2010	Other Postretirement Benefits **2011**	2010
Service cost	**$1,890**	$1,235	**$456**	$428
Interest cost	**10,222**	9,999	**1,909**	2,026
Expected return on plan assets	**(7,990)**	(7,567)	**-**	-
Amortization:				
Transition obligation	**48**	50	**-**	-
Prior service cost/(credit)	**18**	8	**(1,833)**	(1,757)
Net actuarial loss	**2,863**	2,371	**1,506**	1,428
Settlement/curtailment loss/(gain)	**-**	675	**-**	(1,921)
Net periodic benefit costs	**$7,051**	$6,771	**$2,038**	$204

During 2010 a pension plan settlement loss of $0.7 million and a post retirement benefit curtailment gain of $1.9 million were recorded related to restructuring activities.

4. Restructuring

Restructuring charges during 2011 were principally due to organizational changes associated with the substantial completion of the SAP conversion project. The following tables summarize charges reported in the Statement of Operations under Restructuring and other, net for the first six months of 2011 and 2010:

	Six months ending June 30,				
	2011	2010			
(in thousands)	Total restructuring costs*	Total restructuring costs	Termination and other costs	Writedown of plant and equipment	Benefit plan curtailment
Paper Machine Clothing	$481	$2,962	$1,044	$1,243	$675
Albany Door Systems	513	474	474	-	-
Engineered Fabrics	124	607	607	-	-
Engineered Composites	57	-	-	-	-
Unallocated	1,103	(1,962)	(41)	-	(1,921)
Total	$2,278	$2,081	$2,084	$1,243	($1,246)

* Restructuring costs incurred during 2011 pertain to termination and other costs.

The tables below present year-to-date summaries of changes in restructuring liabilities for 2011 and 2010:

(in thousands)	Restructuring charges accrued December 31, 2010	Restructuring accruals in 2011	Payments	Currency translation/ other	Restructuring charges accrued June 30, 2011
Termination costs	$3,443	$1,915	($2,018)	$166	$3,506

(in thousands)	Restructuring charges accrued December 31, 2009	Restructuring accruals in 2010	Payments	Currency translation/ other	Restructuring charges accrued June 30, 2010
Termination costs	$22,067	$1,110	($14,642)	($685)	$7,850

We expect that substantially all accruals for restructuring liabilities as of June 30, 2011 will be paid within one year and therefore have been recorded in current accrued liabilities in the accompanying financial statements.

5. Other Expense/(Income), net

Other expense/(income), net consists of the following:

(in thousands)	Three Months Ended June 30, **2011**	2010	Six Months Ended June 30, **2011**	2010
Currency transactions	**($491)**	($3,933)	**$3,375**	($6,726)
Amortization of debt issuance costs and loan origination fees	**264**	104	**526**	208
Letter of credit fees	**416**	721	**1,272**	1,240
Other miscellaneous (income)/expense	**(134)**	117	**(249)**	6
Total	**$55**	($2,991)	**$4,924**	($5,272)

6. Income Taxes

The following table presents components of income tax expense for the three and six month periods ended June 30, 2011 and 2010:

(in thousands)	Three Months Ended June 30, **2011**	2010	Six Months Ended June 30, **2011**	2010
Income tax expense based on income from continuing operations, at estimated tax rates of 33.0% in 2011 and 32.6% in 2010, respectively	**$4,700**	$7,470	**$12,046**	$10,152
Redemption of life insurance policies	**-**	9,382	**-**	9,382
Provision for change in estimated tax rates	**624**	55	**-**	-
Income tax from continuing operations before discrete items	**$5,324**	$16,907	**$12,046**	$19,534
Discrete tax expense/(benefit):				
Provision for/resolution of tax audits and contingencies	**35**	-	**(1,378)**	-
Repatriation of non-US prior years earnings	**-**	(1,805)	**-**	(1,805)
Total income tax expense	**$5,359**	$15,102	**$10,668**	$17,729

The second-quarter estimated effective tax rate on continuing operations was 33.0% in 2011, as compared to 32.6% for the same period in 2010. The increase in the tax rate was primarily due to a change in the distribution of income and loss among the various countries within which we operate.

We conduct business globally and, as a result, the Company or one or more of our subsidiaries files income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. We are currently under audit in the U.S. and non-U.S. tax jurisdictions, including but not limited to Canada, Germany, France, Japan and Sweden. Tax reserves are recorded for the outcome of these uncertainties in accordance with U.S. GAAP principles.

It is reasonably possible that over the next twelve months the amount of unrecognized tax benefits may change within a range of a net increase of $1.0 million to a net decrease of $12.7 million, from the reevaluation of certain uncertain tax positions arising in examinations, in appeals, or in the courts, or from the closure of tax statutes. Not included in the range is $24.5 million of tax benefits in Germany related to a 1999 reorganization that have been challenged by the German tax authorities in the course of an audit of tax years 2000-2003. In 2008 the German Federal Tax Court denied tax benefits to other taxpayers in a case involving German tax laws relevant to our reorganization. One of these cases involved a non-German party, and in the ruling in that case, the German Federal Tax Court acknowledged that the German law in question may be violative of European Union (EU) principles and referred the issue to the European Court of Justice (ECJ) for its determination. In September 2009, the ECJ issued an opinion in this case that is generally favorable to the other taxpayer and referred the case back to the German Federal Tax Court for further consideration. In May 2010 the German Federal Tax Court released its decision, in which it resolved certain tax issues that may be relevant to our audit and remanded the case to a lower court for further development. Although we were required to pay approximately $15.0 million to the German tax authorities in order to continue to pursue the position, we believe that it is more likely than not that the relevant German law is violative of EU principles and accordingly we have not accrued tax expense on this matter. As we continue to monitor developments it may become necessary for us to accrue tax expense and related interest.

In addition, we received reassessment notices comprised of tax, interest and penalties in the amount of $62.3 million from the Canadian Revenue Agency (CRA) for the tax years 2001 through 2008. Although management continues to believe that the reassessments were substantially without merit and have not accrued tax expense with regard to the full amount of these assessments, we were required to provide letters of credit to the CRA in the amount of $53.2 million and to remit a payment in the amount of $1.8 million in connection with these reassessments. We made the $1.8 million payment to the CRA in July 2011.

7. Earnings Per Share

Earnings per share are computed using the weighted average number of shares of Class A Common Stock and Class B Common Stock outstanding during the period. Diluted earnings per share include the effect of all potentially dilutive securities.

The amounts used in computing earnings per share, including the effect on income and the weighted average number of shares of potentially dilutive securities, are as follows:

(in thousands, except market price data)	Three Months Ended June 30, **2011**	2010	Six Months Ended June 30, **2011**	2010
Net income	**$8,762**	$7,877	**$25,495**	$13,475
Weighted average number of shares:				
Weighted average number of shares used in calculating basic earnings per share	**31,263**	31,058	**31,243**	31,001
Effect of dilutive stock-based compensation awards:				
Stock options	**144**	53	**130**	54
Long-term incentive awards	**82**	50	**82**	50
Weighted average number of shares used in calculating diluted earnings per share	**31,489**	31,161	**31,455**	31,105
Average market price of common stock used for calculation of dilutive shares	**$25.32**	$20.95	**$24.57**	$21.00
Net income per share:				
Basic	**$0.28**	$0.25	**$0.82**	$0.43
Diluted	**$0.28**	$0.25	**$0.81**	$0.43

There was no dilution resulting from the convertible debt instrument, purchased call option, and warrant that are described in Note 10 as of June 30, 2011 and 2010.

The following table presents the number of shares issued and outstanding:

	Class A Shares	Class B Shares	Less: Treasury Shares	Net shares Outstanding

December 31, 2010	36,442,209	3,236,098	(8,484,528)	31,193,779
March 31, 2011	36,505,292	3,236,098	(8,484,528)	31,256,862
June 30, 2011	**36,515,942**	**3,236,098**	**(8,479,487)**	**31,272,553**

8. Inventories

Inventories consist of the following:

(in thousands)	**June 30, 2011**	December 31, 2010
Finished goods	**$78,402**	$71,919
Work in process	**59,238**	48,973
Raw material and supplies	**42,089**	35,279
Total inventories	**$179,729**	$156,171

Inventories are stated at the lower of cost or market and are valued at average cost, net of reserves. We record a provision for obsolete inventory based on the age and category of the inventories.

9. Goodwill and Other Intangible Assets

Goodwill and intangible assets with indefinite useful lives are not amortized, but are tested for impairment at least annually. Goodwill represents the excess of the purchase price over the fair value of the net tangible and identifiable intangible assets acquired in each business combination. Our reporting units are consistent with our operating segments.

Determining the fair value of a reporting unit requires the use of significant estimates and assumptions, including revenue growth rates, operating margins, discount rates, and future market conditions, among others. Goodwill and other long-lived assets are reviewed for impairment whenever events, such as significant changes in the business climate, plant closures, changes in product offerings, or other circumstances indicate that the carrying amount may not be recoverable.

To determine fair value, we utilize two market-based approaches and an income approach. Under the market-based approaches, we utilize information regarding the Company as well as publicly available industry information to determine earnings multiples and sales multiples. Under the income approach, we determine fair value based on estimated future cash flows of each reporting unit, discounted by an estimated weighted-average cost of capital, which reflects the overall level of inherent risk of a reporting unit and the rate of return an outside investor would expect to earn.

We completed our 2011 annual evaluation of goodwill for the Paper Machine Clothing reporting unit and the Albany Door Systems reporting unit in the second quarter of 2011. Our assessment of goodwill impairment indicated that the fair value of each reporting unit exceeded its carrying value and therefore no impairment provision was required.

We are continuing to amortize certain patents, trade names, customer contracts and technology assets that have finite lives. The changes in intangible assets and goodwill from January 1, 2011 to June 30, 2011, were as follows:

(in thousands)	Balance at January 1, 2011	Amortization	Currency translation	Other changes	**Balance at June 30, 2011**
Amortized intangible assets:					
Patents	$221	($179)	$13	-	**$55**
Trade names	48	(2)	-	-	**46**
Customer contracts	3,521	(674)	17	-	**2,864**
Technology	392	(39)	33	-	**386**
Total amortized intangible assets	$4,182	($894)	$63	-	**$3,351**
Unamortized intangible assets:					
Goodwill	$115,616	-	$6,926	-	**$122,542**

As of June 30, 2011, the balance of goodwill was $82.1 million in the Paper Machine Clothing segment and $40.4 million in the Albany Doors Systems segm