DELPHI AUTOMOTIVE SYSTEMS CORP
Form 10-Q
April 19, 2001
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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, DC 20549-1004**

# FORM 10-Q

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

For the quarterly period ended March 31, 2001

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OF THE SECURITIES , EXCHANGE ACT OF 1934

For the transition period from ___________ to ___________

Commission file No. 1-14787

# DELPHI AUTOMOTIVE SYSTEMS CORPORATION

(Exact name of registrant as specified in its charter)

**Delaware**
(State or other jurisdiction of
incorporation or organization) **38-3430473**
(IRS employer
identification number) **5725 Delphi Drive, Troy, Michigan**
(Address of principal executive offices) **48098**
(Zip code)

**(248) 813-2000**

(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 X No _

As of March 31, 2001, there were 559,887,906 outstanding shares of the registrant s $0.01 par value common stock.

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# PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

## DELPHI AUTOMOTIVE SYSTEMS CORPORATION

## CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

| | Three Months Ended March 31, | |
|---|---|---|
| | **2001** | **2000** |
| | **(in millions, except per share amounts)** | |
| Net sales: | | |
| General Motors and affiliates | $4,366 | $5,570 |
| Other customers | 2,169 | 2,234 |
| Total net sales | 6,535 | 7,804 |
| Less operating expenses: | | |
| Cost of sales, excluding items listed below | 5,901 | 6,596 |
| Selling, general and administrative | 378 | 459 |

| | | |
|---|---|---|
| Depreciation and amortization | 317 | 232 |
| Restructuring (Note 2) | 536 | |
| Acquisition-related in-process research and development (Note 3) | | 51 |
| Total operating expenses | 7,132 | 7,338 |
| Operating (loss) income | (597) | 466 |
| Less interest expense | 56 | 40 |
| Other (expense) income, net | (3) | 34 |
| (Loss) income before income taxes | (656) | 460 |
| Income tax (benefit) expense | (227) | 170 |
| Net (loss) income | $(429) | $290 |
| (Loss) earnings per share (Note 1) Basic and diluted | $(0.77) | $0.51 |

See notes to consolidated financial statements.

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## DELPHI AUTOMOTIVE SYSTEMS CORPORATION

## CONSOLIDATED BALANCE SHEETS

| | March 31, 2001 (Unaudited) | December 31, 2000 |
|---|---|---|
| | (in millions) | |
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents | $704 | $760 |
| Accounts receivable, net: | | |
| General Motors and affiliates | 3,178 | 3,308 |
| Other customers | 1,978 | 2,050 |
| Inventories, net (Note 4) | 1,724 | 1,707 |
| Deferred income taxes | 756 | 569 |
| Prepaid expenses and other | 152 | 209 |
| Total current assets | 8,492 | 8,603 |
| Long-term assets: | | |
| Property, net | 5,545 | 5,718 |
| Deferred income taxes | 2,083 | 2,043 |
| Other | 2,435 | 2,157 |
| Total assets | $18,555 | $18,521 |
| **LIABILITIES AND STOCKHOLDERS EQUITY** | | |
| Current liabilities: | | |

| | | |
|---|---|---|
| Notes payable and current portion of long-term debt | $1,477 | $1,559 |
| Accounts payable | 2,895 | 2,871 |
| Restructuring obligations (Note 2) | 486 | |
| Accrued liabilities | 1,597 | 1,813 |
| Total current liabilities | 6,455 | 6,243 |
| Long-term liabilities: | | |
| Long-term debt | 1,891 | 1,623 |
| Postretirement benefits other than pensions | 4,679 | 4,573 |
| Other | 2,308 | 2,316 |
| Total liabilities | 15,333 | 14,755 |
| Stockholders equity (Note 6): | | |
| Common stock, $0.01 par value, 1,350 million shares authorized, 565 million shares issued in 2001 and 2000 | 6 | 6 |
| Additional paid-in capital | 2,450 | 2,450 |
| Retained earnings | 1,401 | 1,869 |
| Other comprehensive income | (541) | (463) |
| Treasury stock, at cost (5.1 million and 5.2 million shares in 2001 and 2000, respectively) | (94) | (96) |
| Total stockholders equity | 3,222 | 3,766 |

| | | |
|---|---|---|
| Total liabilities and stockholders equity | $18,555 | $18,521 |

See notes to consolidated financial statements.



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**DELPHI AUTOMOTIVE SYSTEMS CORPORATION**

**CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)**

| | Three Months Ended March 31, | |
|---|---|---|
| | **2001** | **2000** |
| | **(in millions)** | |
| Cash flows from operating activities: | | |
| Net (loss) income | $(429) | $290 |
| Adjustments to reconcile net (loss) income to net cash provided by (used in) operating activities: | | |
| Depreciation and amortization | 317 | 232 |
| Acquisition-related in-process research and development | | 51 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable, net | 209 | (295) |
| Inventories, net | (11) | 71 |
| Prepaid expenses and other | 53 | 70 |

| | | |
|---|---|---|
| Deferred income taxes | (235) | 121 |
| Accounts payable | 23 | 98 |
| Restructuring obligations | 486 | |
| Accrued liabilities | (215) | (1,314) |
| Other long-term liabilities | 104 | 160 |
| Other | (6) | (4) |
| Net cash provided by (used in) operating activities | 296 | (520) |
| Cash flows from investing activities: | | |
| Capital expenditures | (194) | (275) |
| Cost of acquisitions, net of cash acquired | (263) | (897) |
| Other | 37 | (28) |
| Net cash used in investing activities | (420) | (1,200) |
| Cash flows from financing activities: | | |
| Net proceeds from issuance of debt securities and borrowings under credit facilities and other debt | 185 | 1,155 |
| Dividend payments | (39) | (39) |
| Purchase of treasury stock | | (7) |

| | | |
|---|---|---|
| Net cash provided by financing activities | 146 | 1,109 |
| Effect of exchange rate fluctuations on cash and cash equivalents | (78) | (19) |
| Decrease in cash and cash equivalents | (56) | (630) |
| Cash and cash equivalents at beginning of period | 760 | 1,546 |
| Cash and cash equivalents at end of period | $704 | $916 |

See notes to consolidated financial statements.



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**DELPHI AUTOMOTIVE SYSTEMS CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)**

## 1. BASIS OF PRESENTATION

***General*** Delphi Automotive Systems Corporation ( Delphi ) is a world-leading supplier of vehicle electronics, transportation components, integrated systems and modules. The consolidated financial statements and notes thereto included in this report should be read in conjunction with our consolidated financial statements and notes thereto included in our 2000 Annual Report on Form 10-K filed with the Securities and Exchange Commission. The consolidated financial statements include the accounts of Delphi and its wholly owned and majority owned subsidiaries.

All significant intercompany transactions and balances between consolidated Delphi businesses have been eliminated. In the opinion of management, all adjustments, consisting of only normal recurring items, which are necessary for a fair presentation have been included. The results for interim periods are not necessarily indicative of results which may be expected from any other interim period or for the full year and may not necessarily reflect the consolidated results of operations, financial position and cash flows of Delphi in the future.

Certain prior period amounts have been reclassified to conform with the current period presentation.

***Earnings Per Share*** Basic earnings per share amounts were computed using weighted average shares outstanding for each respective period. Diluted earnings per share also reflect the weighted average impact from the date of issuance of all potentially dilutive securities during the periods presented, except for the three months ended March 31, 2001, where such inclusion would have had an antidilutive effect. Actual weighted average shares outstanding used in calculating basic and diluted earnings per share were:

| | Three Months Ended March 31, 2001 | Three Months Ended March 31, 2000 |
|---|---|---|
| | (in thousands) | |
| Weighted average shares outstanding | 559,835 | 562,546 |
| Effect of dilutive securities | | 2,976 |
| Diluted shares outstanding | 559,835 | 565,522 |

The Board of Directors declared a dividend on Delphi common stock of $0.07 per share on March 7, 2001, payable on April 16, 2001 to holders of record on March 19, 2001. The dividend declared on December 6, 2000 was paid on January 18, 2001.

## 2. RESTRUCTURING AND IMPAIRMENT CHARGES

In the first quarter of 2001, Delphi approved plans to sell, close or consolidate nine plants, downsize the workforce at more than 40 other facilities and exit selected products within the next twelve months. We also impaired certain long-lived assets at impacted sites and certain investments in joint ventures. As a result of these actions, we recorded a total charge of $617 million ($404 million after-tax).

The restructuring charge of $536 million includes $492 million of employee costs (including postemployment benefits and special termination pension benefits) and $44 million in other exit costs (principally lease termination and contract cancellation payments). The plans entail the elimination of approximately 11,500 positions worldwide, comprised of 5,600 U.S. hourly employees, 2,000 U.S. salaried employees, and 3,900 employees in non-U.S. locations. Employees at impacted locations have been informed of the restructuring initiatives and benefits available to them under applicable benefit plans or related contractual provisions have been communicated. Affected employees will leave Delphi using a mixture of voluntary and involuntary separation programs, early retirements, social plan programs and layoffs. Excluding special termination pension benefits, we expect to pay approximately $450 million in cash related to the restructuring plans. During the first quarter of 2001, we paid $49 million related to





employee costs and $1 million in other exit costs. As of March 31, 2001, approximately 2,000 employees had been separated under the plans.

We have evaluated the carrying value of the long-lived assets at each impacted site for impairment. The carrying value of a long-lived asset is considered impaired when the anticipated separately identifiable undiscounted cash flows from that asset are less than the carrying value of the asset. We recorded impairment losses of $63 million in depreciation and amortization, primarily related to machinery and equipment held for use in the Safety, Thermal and Electrical Architecture sector. The impairment losses were determined based on the amount by which the carrying value exceeded the fair market value of the asset. Fair market value was determined primarily using the anticipated discounted cash flows.

In addition, we recorded impairment charges of $18 million related to permanent declines in the value of our investments in certain joint ventures. These charges, included in other expense, primarily related to certain Korean joint ventures as more fully explained in Note 8.

## 3. ACQUISITIONS

### *Delphi Mechatronic Systems*

On March 30, 2001, Delphi acquired substantially all of the assets and assumed certain liabilities of Eaton Corporation s Vehicle Switch/ Electronics Division, now Delphi Mechatronic Systems, for approximately $0.3 billion. The acquisition was funded with short-term borrowings under Delphi s existing commercial paper program as well as uncommitted lines of credit, which we expect to refinance on a long-term basis. The purchase price is subject to adjustment for certain post-closing events including governmental approval of the transfer of certain assets in Poland. Delphi Mechatronic Systems is a global producer of electromechanical switches, mechatronic modules and body electronics for the light vehicle industry with 2000 sales of $320 million, primarily in North America. Delphi Mechatronic Systems technology, complemented by our extensive electrical and electronic integration capabilities, will enable us to offer customers new solutions in modular cockpits, doors and overhead systems. The Delphi Mechatronic Systems acquisition supports our goals of enhancing our technology, diversifying our customer base and geographic footprint, and leveraging our system integration capabilities. The acquisition is accounted for using the purchase method of accounting and therefore, the purchase price will be allocated to assets acquired and liabilities assumed based on estimated fair values. The final purchase price allocation has not been determined. As the transaction closed on March 30, 2001, there was no impact on our first quarter 2001 results of operations.

### *Delphi Diesel Systems*

In January 2000, Delphi purchased Lucas Diesel Systems, now Delphi Diesel Systems, for $0.8 billion, net of cash acquired. Delphi Diesel Systems is one of the world s largest producers of diesel fuel-injection systems for light, medium and heavy-duty vehicles. The acquisition was accounted for using the purchase method of accounting and, therefore, the purchase price was allocated to assets acquired and liabilities assumed based on estimated fair values. The results of operations of Delphi Diesel Systems are included in our consolidated financial statements from the acquisition date. The $345 million excess of the consideration given over the estimated fair value of net assets acquired has been recorded as goodwill and is being amortized over 20 years. In conjunction with the acquisition of Delphi Diesel Systems during the first quarter of 2000, we recognized a one-time, non-cash charge to earnings of $51 million ($32 million after-tax) resulting from acquisition-related in-process research and development that had not reached technological feasibility and had no alternative use.

***Delphi Lockheed Automotive***

In February 2000, Delphi purchased Automotive Products Distribution Services, now Delphi Lockheed Automotive, for $63 million. Delphi Lockheed Automotive is a leading European distributor of automotive aftermarket products for passenger cars and commercial vehicles.



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The pro forma effects of these acquisitions would not be significantly different from reported results.

## 4. INVENTORIES, NET

Inventory, net consisted of:

| | March 31, 2001 | December 31, 2000 |
|---|---|---|
| | (in millions) | |
| Productive material, work-in-process and supplies | $1,712 | $1,689 |
| Finished goods | 308 | 314 |
| Total inventories at FIFO | 2,020 | 2,003 |
| Less allowance to adjust the carrying value of certain inventories to LIFO | (296) | (296) |
| Total inventories, net | $1,724 | $1,707 |

**5. DERIVATIVES AND HEDGING ACTIVITIES**

Effective January 1, 2001, Delphi adopted Statement of Financial Accounting Standards (SFAS) No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended, which requires that all derivative instruments be reported on the balance sheet at fair value and establishes criteria for designation and effectiveness of transactions entered into for hedging purposes. The cumulative effect of adopting SFAS No. 133 was to increase other comprehensive income ( OCI ) by $14 million, after-tax. The effect on net income was not significant, primarily because the hedges in place as of January 1, 2001 qualified for hedge accounting treatment and were highly effective.

Delphi is exposed to market risk, such as fluctuations in foreign currency exchange rates, commodity prices and changes in interest rates. To manage the volatility relating to these exposures, we aggregate the exposures on a consolidated basis to take advantage of natural offsets. For exposures that are not offset within our operations, we enter into various derivative transactions pursuant to our risk management policies. Designation is performed on a transaction basis to support hedge accounting. The changes in fair value of these hedging instruments are offset in part or in whole by corresponding changes in the fair value or cash flows of the underlying exposures being hedged. We assess the initial and ongoing effectiveness of our hedging relationships in accordance with our documented policy. We do not hold or issue derivative financial instruments for trading purposes.

Delphi has foreign currency exchange exposure from buying and selling in currencies other than the local currencies of our operating units. The primary purpose of our foreign currency hedging activities is to manage the volatility associated with forecasted foreign currency purchases and sales. Principal currencies hedged include the Mexican peso, Canadian dollar, European euro, Japanese yen, Singapore dollar, and Brazilian real. We primarily utilize forward exchange contracts with maturities of less than 18 months, which qualify as cash flow hedges.

Delphi has exposure to the prices of commodities in its procurement of certain raw materials. The primary purpose of our commodity price hedging activities is to manage the volatility associated with these forecasted inventory purchases. We primarily utilize swaps and options with maturities of less than 24 months, which qualify as cash flow hedges. These instruments are intended to offset the effect of changes in commodity prices on forecasted inventory purchases.

In order to manage the interest rate risk associated with our debt portfolio, we enter into derivative transactions to manage our exposure to changes in interest rates. Our interest rate derivatives mature within the next six months and qualify as cash flow hedges.

Gains and losses on derivatives qualifying as cash flow hedges are recorded in OCI to the extent that hedges are effective until the underlying transactions are recognized in earnings. Net gains included in OCI as of March 31, 2001, including the transition adjustment, were $9 million after-tax ($14 million





pre-tax). Of this pre-tax total, a gain of approximately $16 million will be included in cost of sales within the next 12 months, a loss of approximately $6 million will be included in depreciation and amortization expense over the lives of the related fixed assets and a gain of approximately $4 million will be included in interest expense over the term of the related debt. The unrealized amounts in OCI will fluctuate based on changes in the fair value of open contracts at each reporting period. Due to unusually pronounced production volume reductions, we discontinued several cash flow hedges during the quarter ended March 31, 2001, which resulted in the immediate recognition of $6 million of income included in cost of sales. Cash flow hedges are discontinued when it is probable that the original forecasted transactions will not occur. The amount included in cost of sales related to hedge ineffectiveness and the time value of options was not significant.

In 2000, we entered into certain commodity derivative instruments to protect against commodity price changes related to forecasted inventory purchases. Although these derivatives are effective as economic hedges of our commodity price exposures, due to differences in pricing terms between the derivative instruments and the forecasted purchases, the SFAS No. 133 effectiveness threshold was not met. The change in fair value of these instruments was included in cost of sales as of March 31, 2001, but was not significant. These contracts settle during 2001. We have changed the pricing terms of the related commodity purchases such that future hedges are expected to qualify for hedge accounting.

## 6. STOCKHOLDERS EQUITY

Changes in stockholders equity for the three months ended March 31, 2001 were:

| | Common Stock | | Additional | | Other | | Total |
|---|---|---|---|---|---|---|---|
| | | | Paid-in | Retained | Comprehensive | Treasury | Stockholders |
| | Shares | Amount | Capital | Earnings | Income | Stock | Equity |
| | (in millions) | | | | | | |
| Balance at January 1, 2001 | 565 | $6 | $2,450 | $1,869 | $(463) | $(96) | $3,766 |
| Net loss | | | | (429) | | | (429) |
| Foreign currency translation adjustments, net of tax | | | | | (87) | | (87) |
| Cumulative effect of accounting change, net of tax (Note 5) | | | | | 14 | | 14 |
| Net change in unrecognized gain on derivative instruments, net of tax | | | | | (5) | | (5) |
| Total comprehensive income | | | | | | | (507) |
| Net shares reacquired for employee benefit plans | | | | | | 2 | 2 |
| Dividends | | | | (39) | | | (39) |
| Balance at March 31, 2001 | 565 | $6 | $2,450 | $1,401 | $(541) | $(94) | $3,222 |

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**7. SEGMENT REPORTING**

Selected information regarding Delphi s product sectors follows: