

POLYONE CORP
Form 10-Q
April 17, 2019

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 March 31, 2019

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 1-16091

POLYONE CORPORATION
(Exact name of registrant as specified in its charter)

Ohio 34-1730488
(State or other jurisdiction (I.R.S. Employer Identification No.)
of incorporation or organization)

33587 Walker Road, Avon Lake, Ohio 44012
(Address of principal executive offices) (Zip Code)
Registrant's telephone number, including area code: (440) 930-1000

Former name, former address and former fiscal year, if changed since last report: Not Applicable
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 every Interactive Data File required to be submitted 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 such files). Yes No
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.
Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company
Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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 the registrant's outstanding common shares, \$0.01 par value, as of March 31, 2019 was 77,815,154.

PART I — FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

PolyOne Corporation

Condensed Consolidated Statements of Income (Unaudited)

(In millions, except per share data)

	Three Months Ended March 31,	
	2019	2018
Sales	\$899.9	\$901.6
Cost of sales	703.6	703.1
Gross margin	196.3	198.5
Selling and administrative expense	128.0	119.7
Operating income	68.3	78.8
Interest expense, net	(15.9)	(15.5)
Other income, net	0.2	1.1
Income from continuing operations before income taxes	52.6	64.4
Income tax expense	(14.3)	(16.7)
Net income from continuing operations	38.3	47.7
Loss from discontinued operations, net of income taxes	—	(0.8)
Net income	\$38.3	\$46.9
Net income attributable to noncontrolling interests	(0.1)	—
Net income attributable to PolyOne common shareholders	\$38.2	\$46.9
Earnings (loss) per common share attributable to PolyOne common shareholders - Basic:		
Continuing operations	\$0.49	\$0.59
Discontinued operations	—	(0.01)
Total	\$0.49	\$0.58
Earnings (loss) per common share attributable to PolyOne common shareholders - Diluted:		
Continuing operations	\$0.49	\$0.59
Discontinued operations	—	(0.01)
Total	\$0.49	\$0.58
Weighted-average shares used to compute earnings per common share:		
Basic	77.8	80.4
Plus dilutive impact of share-based compensation	0.4	0.9
Diluted	78.2	81.3
Anti-dilutive shares not included in diluted common shares outstanding	0.9	0.1
Cash dividends declared per share of common stock	\$0.195	\$0.175

See accompanying Notes to the Unaudited Condensed Consolidated Financial Statements.

PolyOne Corporation
 Consolidated Statements of Comprehensive Income (Unaudited)
 (In millions)

	Three Months Ended March 31,	
	2019	2018
Net income	\$38.3	\$46.9
Other comprehensive income, net of tax		
Translation adjustments and related hedging instruments	4.2	10.6
Cash flow hedges	(1.0)	—
Total comprehensive income	41.5	57.5
Comprehensive income attributable to noncontrolling interests	(0.1)	—
Comprehensive income attributable to PolyOne common shareholders	\$41.4	\$57.5

See accompanying Notes to the Unaudited Condensed Consolidated Financial Statements.

PolyOne Corporation
Condensed Consolidated Balance Sheets
(In millions)

	(Unaudited) March 31, 2019	December 31, 2018
Assets		
Current assets:		
Cash and cash equivalents	\$ 108.3	\$ 170.9
Accounts receivable, net	480.2	413.4
Inventories, net	374.9	344.7
Other current assets	71.3	69.8
Total current assets	1,034.7	998.8
Property, net	497.1	495.4
Goodwill	705.5	650.3
Intangible assets, net	492.4	423.4
Operating lease assets, net	76.6	—
Other non-current assets	155.5	155.4
Total assets	\$ 2,961.8	\$ 2,723.3
Liabilities and Equity		
Current liabilities:		
Short-term and current portion of long-term debt	\$ 19.0	\$ 19.4
Accounts payable	407.2	399.0
Current operating lease obligations	23.2	—
Accrued expenses and other current liabilities	120.9	139.2
Total current liabilities	570.3	557.6
Non-current liabilities:		
Long-term debt	1,440.7	1,336.2
Pension and other post-retirement benefits	54.0	54.3
Non-current operating lease obligations	53.4	—
Other non-current liabilities	274.5	234.6
Total non-current liabilities	1,822.6	1,625.1
Equity:		
PolyOne shareholders' equity	568.2	540.0
Noncontrolling interests	0.7	0.6
Total equity	568.9	540.6
Total liabilities and equity	\$ 2,961.8	\$ 2,723.3

See accompanying Notes to the Unaudited Condensed Consolidated Financial Statements.

PolyOne Corporation
Condensed Consolidated Statements of Cash Flows (Unaudited)
(In millions)

	Three Months Ended March 31,	
	2019	2018
Operating Activities		
Net income	\$38.3	\$46.9
Adjustments to reconcile net income to net cash (used) provided by operating activities:		
Depreciation and amortization	23.3	22.4
Share-based compensation expense	2.5	2.7
Change in assets and liabilities, net of the effect of acquisitions:		
Increase in accounts receivable	(53.0)	(82.4)
(Increase) decrease in inventories	(12.0)	17.0
Increase in accounts payable	1.2	16.6
Decrease in pension and other post-retirement benefits	(1.9)	(2.3)
(Decrease) increase in accrued expenses and other assets and liabilities, net	(23.1)	5.8
Net cash (used) provided by operating activities	(24.7)	26.7
Investing Activities		
Capital expenditures	(9.9)	(12.9)
Business acquisitions, net of cash acquired	(119.6)	(73.0)
Sale of and proceeds from other assets	1.6	—
Net cash used by investing activities	(127.9)	(85.9)
Financing Activities		
Borrowings under credit facilities	374.7	286.6
Repayments under credit facilities	(269.2)	(249.1)
Purchase of common shares for treasury	—	(42.2)
Cash dividends paid	(15.6)	(14.2)
Repayment of long-term debt	(1.6)	(1.6)
Payments of withholding tax on share awards	(1.3)	(1.6)
Net cash provided (used) by financing activities	87.0	(22.1)
Effect of exchange rate changes on cash	3.0	3.2
Decrease in cash and cash equivalents	(62.6)	(78.1)
Cash and cash equivalents at beginning of period	170.9	243.6
Cash and cash equivalents at end of period	\$108.3	\$165.5

See accompanying Notes to the Unaudited Condensed Consolidated Financial Statements.

PolyOne Corporation
 Consolidated Statements of Shareholders' Equity (Unaudited)
 (In millions)

	Common Shares		Shareholders' Equity			Common Shares Held in Treasury	Accumulated Other Comprehensive Loss	Total PolyOne Shareholders' equity	Non-contr Interests	Total equity
	Common Shares	Shares Held in Treasury	Common Shares	Additional Paid-in Capital	Retained Earnings					
Balance at January 1, 2019	122.2	(44.5)	\$ 1.2	\$ 1,166.9	\$ 472.9	\$(1,018.7)	\$ (82.3)	\$ 540.0	\$ 0.6	\$ 540.6
Net income					38.2			38.2	0.1	38.3
Other comprehensive gain							3.2	3.2		3.2
Cash dividends declared					(14.8)			(14.8)		(14.8)
Repurchase of common shares								—		—
Share-based compensation and exercise of awards	0.1		0.5			1.1		1.6		1.6
Balance at March 31, 2019	122.2	(44.4)	\$ 1.2	\$ 1,167.4	\$ 496.3	\$(1,017.6)	\$ (79.1)	\$ 568.2	\$ 0.7	\$ 568.9
	Common Shares		Shareholders' Equity			Common Shares Held in Treasury	Accumulated Other Comprehensive Loss	Total PolyOne Shareholders' equity	Non-contr Interests	Total equity
	Common Shares	Shares Held in Treasury	Common Shares	Additional Paid-in Capital	Retained Earnings					
Balance at January 1, 2018	122.2	(41.3)	\$ 1.2	\$ 1,161.5	\$ 387.1	\$(898.3)	\$ (53.0)	\$ 598.5	\$ 0.9	\$ 599.4
Net income					46.9			46.9		46.9
Other comprehensive gain							10.6	10.6		10.6
Cash dividends declared					(14.0)			(14.0)		(14.0)
Repurchase of common shares		(1.0)				(42.2)		(42.2)		(42.2)
Share-based compensation and exercise of awards	0.1		0.2			1.2		1.4		1.4
Other					(16.6)		(0.4)	(17.0)		(17.0)
Balance at March 31, 2018	122.2	(42.2)	\$ 1.2	\$ 1,161.7	\$ 403.4	\$(939.3)	\$ (42.8)	\$ 584.2	\$ 0.9	\$ 585.1

See accompanying Notes to the Unaudited Condensed Consolidated Financial Statements.

PolyOne Corporation

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note 1 — BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with Form 10-Q instructions and in the opinion of management contain all adjustments, including those that are normal, recurring and necessary to present fairly the financial position, results of operations and cash flows for the periods presented. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates. These interim financial statements should be read in conjunction with the financial statements and accompanying notes included in the annual report on Form 10-K for the year ended December 31, 2018 of PolyOne Corporation. When used in this quarterly report on Form 10-Q, the terms “we,” “us,” “our,” “PolyOne” and the “Company” mean PolyOne Corporation and its consolidated subsidiaries. Operating results for the three months ended March 31, 2019 are not necessarily indicative of the results that may be attained in subsequent periods or for the year ending December 31, 2019.

Accounting Standards Adopted

On January 1, 2019, the Company adopted Accounting Standards Codification (ASC) 842, Leases. ASC 842 was issued to increase transparency and comparability among entities by recognizing right-of-use assets and lease liabilities on the balance sheet and disclosing key information about lease arrangements.

We elected to transition to ASC 842 using the option to apply the standard on its effective date, January 1, 2019. The comparative periods presented reflect the former lease accounting guidance and the required comparative disclosures are included in Note 4, Leasing Arrangements. There was not a material cumulative-effect adjustment to our beginning retained earnings as a result of adopting ASC 842. We have recognized additional operating lease assets and obligations of \$72.3 million and \$76.6 million as of January 1, 2019 and March 31, 2019, respectively. We elected to not reassess prior conclusions related to the identification, classification and accounting for initial direct costs for leases that commenced prior to January 1, 2019. Additionally, we elected to not use hindsight to determine lease terms and to not separate non-lease components within our lease portfolio. For additional disclosure and detail, see Note 4, Leasing Arrangements.

Accounting Standards Not Yet Adopted

In June 2016, the Financial Accounting Standards Board (FASB) issued ASU 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments (ASU 2016-13). ASU 2016-13 changes the impairment model for most financial instruments. Current guidance requires the recognition of credit losses based on an incurred loss impairment methodology that reflects losses once the losses are probable. Under ASU 2016-13, the Company will be required to use a current expected credit loss model (CECL) that will immediately recognize an estimate of credit losses that are expected to occur over the life of the financial instruments that are in the scope of this update, including trade receivables. The CECL model uses a broader range of reasonable and supportable information in the development of credit loss estimates. This guidance becomes effective for the Company on January 1, 2020, including the interim periods in the year. The Company is currently evaluating the impact that the adoption of this ASU will have on the consolidated financial statements and related disclosures.

Note 2 — BUSINESS COMBINATIONS

On January 2, 2019, the Company acquired Fiber-Line, LLC (Fiber-Line), a global leader in polymer coated engineered fibers and composite materials, for total consideration of \$152.7 million, net of cash acquired and inclusive of contingent consideration. The contingent consideration is calculated over a two-year period where each year's earnings before interest, taxes, depreciation, and amortization (EBITDA) must exceed "baseline EBITDA." Fiber-Line's results are reported in the Specialty Engineered Materials segment. The preliminary purchase price allocation resulted in intangible assets of \$77.4 million, goodwill of \$55.1 million, and net working capital of \$26.0 million. A portion of the goodwill is deductible for U.S. federal income tax purposes. The intangible assets that have been acquired are being amortized over a period of five to 20 years. Fiber-Line's sales included in the Company's results for the three months ended March 31, 2019 were \$26.8 million.

Note 3 — GOODWILL AND INTANGIBLE ASSETS

Goodwill as of March 31, 2019 and December 31, 2018 and changes in the carrying amount of goodwill by segment were as follows:

(In millions)	Specialty Engineered Materials	Color, Additives and Inks	Performance Products and Solutions	PolyOne Distribution	Total
Balance December 31, 2018	\$ 188.9	\$ 448.6	\$ 11.2	\$ 1.6	\$650.3
Acquisition of businesses	55.9	—	—	—	55.9
Currency translation	(0.2)	(0.5)	—	—	(0.7)
Balance March 31, 2019	\$ 244.6	\$ 448.1	\$ 11.2	\$ 1.6	\$705.5

Indefinite and finite-lived intangible assets consisted of the following:

As of March 31, 2019					
(In millions)	Acquisition Cost	Accumulated Amortization	Currency Translation	Net	
Customer relationships	\$290.7	\$ (79.3)	\$ (1.1)	\$210.3	
Patents, technology and other	253.2	(70.1)	(1.3)	181.8	
Indefinite-lived trade names	100.3	—	—	100.3	
Total	\$644.2	\$ (149.4)	\$ (2.4)	\$492.4	
As of December 31, 2018					
(In millions)	Acquisition Cost	Accumulated Amortization	Currency Translation	Net	
Customer relationships	\$278.4	\$ (75.0)	\$ (0.7)	\$202.7	
Patents, technology and other	188.1	(66.8)	(0.9)	120.4	
Indefinite-lived trade names	100.3	—	—	100.3	
Total	\$566.8	\$ (141.8)	\$ (1.6)	\$423.4	

Note 4 — LEASING ARRANGEMENTS

We lease certain manufacturing facilities, warehouse space, machinery and equipment, vehicles and information technology equipment under operating leases. The majority of our leases are operating leases. Finance leases are immaterial to our condensed consolidated financial statements. Operating lease assets and obligations are reflected within Operating lease assets, net, Current operating lease obligations, and Non-current operating lease obligations, respectively, on the Condensed Consolidated Balance Sheet.

Lease expense for these leases is recognized on a straight-line basis over the lease term, with variable lease payments recognized in the period those payments are incurred. The components of lease cost recognized within our Condensed Consolidated Statements of Income were as follows:

(In millions)	Condensed Consolidated Statements of Income Location	Three Months Ended March 31, 2019
Lease cost:		
Operating lease cost	Cost of sales	\$ 3.4
Operating lease cost	Selling and administrative expense	2.7
Other ⁽¹⁾	Selling and administrative expense	0.7
Total operating lease cost		\$ 6.8

(1) Other lease costs include short-term lease costs and variable lease costs

We often have options to renew lease terms for buildings and other assets. The exercise of lease renewal options are generally at our sole discretion. In addition, certain lease arrangements may be terminated prior to their original

expiration date at our discretion. We evaluate renewal and termination options at the lease commencement date to determine if we are reasonably certain to exercise the option on the basis of economic factors. The weighted average remaining lease term for our operating leases as of March 31, 2019 was 4.3 years.

The discount rate implicit within our leases is generally not determinable and therefore the Company determines the discount rate based on its incremental borrowing rate. The incremental borrowing rate for our leases is determined based on lease term and currency in which lease payments are made, adjusted for impacts of collateral. The weighted average discount rate used to measure our operating lease liabilities as of March 31, 2019 was 5.7%.

Maturity Analysis of Lease Liabilities:

(In millions)	As of March 31, 2019 Operating Leases
2019	\$ 19.9
2020	22.3
2021	14.2
2022	10.1
2023	7.5
Thereafter	8.9
Total lease payments	\$ 82.9
Less amount of lease payment representing interest	(6.3)
Total present value of lease payments	\$ 76.6

(In millions)	As of December 31, 2018 Operating Leases
2019	\$ 24.5
2020	20.4
2021	12.4
2022	8.5
2023	5.8
Thereafter	9.0
Total	\$ 80.6

Note 5 — INVENTORIES, NET

Components of Inventories, net are as follows:

(In millions)	As of March 31, 2019	As of December 31, 2018
Finished products	\$ 224.2	\$ 204.3
Work in process	8.6	6.9
Raw materials and supplies	142.1	133.5
Inventories, net	\$ 374.9	\$ 344.7

Note 6 — PROPERTY, NET

Components of Property, net are as follows:

(In millions)	As of March 31, 2019	As of December 31, 2018
Land and land improvements	\$ 48.6	