Sensata Technologies Holding N.V.
Form 10-Q
July 29, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2014

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 001-34652

SENSATA TECHNOLOGIES HOLDING N.V.
(Exact Name of Registrant as Specified in Its Charter)

THE NETHERLANDS (State or other jurisdiction of incorporation or organization)	98-0641254 (I.R.S. Employer Identification No.)
Kolthofsingel 8, 7602 EM Almelo The Netherlands	31-546-879-555
(Address of Principal Executive Offices, including Zip Code)	(Registrant’s Telephone Number, Including Area Code)

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 ý 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 ý 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 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 ý		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 ý

As of July 15, 2014, 168,361,657 ordinary shares were outstanding.

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PART I—FINANCIAL INFORMATION

Item 1. Financial Statements.
SENSATA TECHNOLOGIES HOLDING N.V.
Condensed Consolidated Balance Sheets
(In thousands, except per share amounts)
(unaudited)

	June 30, 2014	December 31, 2013
Assets		
Current assets:		
Cash and cash equivalents	$184,638	$317,896
Accounts receivable, net of allowances of $9,308 and $9,199 as of June 30, 2014 and December 31, 2013, respectively	352,623	291,723
Inventories	226,058	183,395
Deferred income tax assets	21,817	20,975
Prepaid expenses and other current assets	33,051	41,642
Total current assets	818,187	855,631
Property, plant and equipment, at cost	752,636	675,690
Accumulated depreciation	(360,166)	(331,033)
Property, plant and equipment, net	392,470	344,657
Goodwill	1,787,224	1,756,049
Other intangible assets, net of accumulated amortization of $1,144,172 and $1,079,595 as of June 30, 2014 and December 31, 2013, respectively	513,427	502,388
Deferred income tax assets	9,992	10,623
Deferred financing costs	17,329	19,132
Other assets	11,595	10,344
Total assets	$3,550,224	$3,498,824
Liabilities and shareholders’ equity		
Current liabilities:		
Current portion of long-term debt, capital lease and other financing obligations	$7,984	$8,100
Accounts payable	223,163	177,539
Income taxes payable	7,679	5,785
Accrued expenses and other current liabilities	135,929	123,239
Deferred income tax liabilities	3,859	3,829
Total current liabilities	378,614	318,492
Deferred income tax liabilities	307,653	281,364
Pension and post-retirement benefit obligations	19,568	19,508
Capital lease and other financing obligations, less current portion	47,359	48,845
Long-term debt, net of discount, less current portion	1,664,812	1,667,021
Other long-term liabilities	18,102	22,006
Commitments and contingencies		
Total liabilities	2,436,108	2,357,236
Shareholders’ equity:		
Ordinary shares, €0.01 nominal value per share, 400,000 shares authorized; 178,437 shares issued as of June 30, 2014 and December 31, 2013	2,289	2,289
Treasury shares, at cost, 10,075 and 6,462 shares as of June 30, 2014 and December 31, 2013, respectively	(395,424)	(236,346)
Additional paid-in capital	1,603,162	1,596,544

Accumulated deficit	(66,657)	(187,792)
Accumulated other comprehensive loss	(29,254)	(33,107)
Total shareholders’ equity	1,114,116	1,141,588
Total liabilities and shareholders’ equity	$3,550,224	$3,498,824

The accompanying notes are an integral part of these condensed consolidated financial statements.

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SENSATA TECHNOLOGIES HOLDING N.V.
Condensed Consolidated Statements of Operations
(In thousands, except per share amounts)
(unaudited)

	For the three months ended		For the six months ended	
	June 30, 2014	June 30, 2013	June 30, 2014	June 30, 2013
Net revenue	$575,853	$506,418	$1,127,447	$976,831
Operating costs and expenses:				
Cost of revenue	368,446	322,699	725,645	631,381
Research and development	18,492	14,308	36,156	27,924
Selling, general and administrative	50,638	42,821	95,310	81,075
Amortization of intangible assets	32,561	33,650	64,577	67,036
Restructuring and special charges	1,740	2,350	2,605	4,026
Total operating costs and expenses	471,877	415,828	924,293	811,442
Profit from operations	103,976	90,590	203,154	165,389
Interest expense	(23,587)	(23,962)	(47,099)	(48,097)
Interest income	281	400	589	548
Other, net	3,932	(32,200)	4,470	(34,801)
Income before taxes	84,602	34,828	161,114	83,039
Provision for income taxes	20,709	14,457	28,848	28,003
Net income	$63,893	$20,371	$132,266	$55,036
Basic net income per share:	$0.37	$0.12	$0.77	$0.31
Diluted net income per share:	$0.37	$0.11	$0.76	$0.31

The accompanying notes are an integral part of these condensed consolidated financial statements.

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SENSATA TECHNOLOGIES HOLDING N.V.
Condensed Consolidated Statements of Comprehensive Income
(In thousands)
(unaudited)

	For the three months ended		For the six months ended	
	June 30, 2014	June 30, 2013	June 30, 2014	June 30, 2013
Net income	$63,893	$20,371	$132,266	$55,036
Other comprehensive income/(loss), net of tax:				
Net unrealized gain/(loss) on derivative instruments designated and qualifying as cash flow hedges	1,888	(1,759)	4,053	6,848
Amortization of net loss and prior service (credit)/cost on defined benefit and retiree healthcare plans	(129)	418	(200)	872
Other comprehensive income/(loss)	1,759	(1,341)	3,853	7,720
Comprehensive income	$65,652	$19,030	$136,119	$62,756

The accompanying notes are an integral part of these condensed consolidated financial statements.

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SENSATA TECHNOLOGIES HOLDING N.V.
Condensed Consolidated Statements of Cash Flows
(In thousands)
(unaudited)

	For the six months ended	
	June 30, 2014	June 30, 2013
Cash flows from operating activities:		
Net income	$132,266	$55,036
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	30,209	25,361
Amortization of deferred financing costs and original issue discounts	2,386	2,263
Currency remeasurement loss/(gain) on debt	49	(185)
Share-based compensation	6,351	4,602
Loss on debt refinancing	—	7,111
Amortization of inventory step-up to fair value	907	—
Amortization of intangible assets	64,577	67,036
(Gain)/loss on disposition of assets	(578)	806
Deferred income taxes	16,695	12,621
Gains from insurance proceeds	(2,417)	—
Unrealized (gain)/loss on hedges and other non-cash items	(3,475)	24,037
Changes in operating assets and liabilities, net of effects of acquisitions:		
Accounts receivable, net	(49,044)	(51,849)
Inventories	(30,796)	2,684
Prepaid expenses and other current assets	4,444	1,681
Accounts payable and accrued expenses	43,381	33,030
Income taxes payable	1,894	2,120
Other	526	(6,228)
Net cash provided by operating activities	217,375	180,126
Cash flows from investing activities:		
Additions to property, plant and equipment and capitalized software	(67,199)	(33,853)
Insurance proceeds	2,417	1,400
Proceeds from sale of assets	5,467	—
Acquisition payments, net of cash received	(117,085)	(411)
Net cash used in investing activities	(176,400)	(32,864)
Cash flows from financing activities:		
Proceeds from exercise of stock options and issuance of ordinary shares	11,197	11,163
Proceeds from issuance of debt	35,000	500,000
Payments on debt	(39,291)	(706,658)
Repurchase of ordinary shares from SCA	(169,680)	—
Payments to repurchase ordinary shares	(11,459)	(125,218)
Payments of debt issuance costs	—	(5,741)
Net cash used in financing activities	(174,233)	(326,454)
Net change in cash and cash equivalents	(133,258)	(179,192)
Cash and cash equivalents, beginning of period	317,896	413,539
Cash and cash equivalents, end of period	$184,638	$234,347

The accompanying notes are an integral part of these condensed consolidated financial statements.

SENSATA TECHNOLOGIES HOLDING N.V.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(In thousands, except per share amounts, or unless otherwise noted)
(unaudited)

1. Business Description and Basis of Presentation

Business Description

The accompanying unaudited condensed consolidated financial statements presented herein reflect the financial position, results of operations, comprehensive income, and cash flows of Sensata Technologies Holding N.V. and its wholly-owned subsidiaries, collectively referred to as the “Company,” “Sensata,” “we,” “our,” or “us.”

We are incorporated under the laws of the Netherlands. We conduct our operations through subsidiary companies that operate business and product development centers in the United States (the “U.S.”), the Netherlands, Belgium, China, and Japan; and manufacturing operations in China, South Korea, Malaysia, Mexico, the Dominican Republic, Bulgaria, and the U.S. We organize our operations into the sensors and controls businesses.

Our sensors business is a manufacturer of pressure, temperature, speed, position, and force sensors, and electromechanical products used in subsystems of automobiles (e.g., engine, air conditioning, and ride stabilization), heavy on- and off-road vehicles, and in industrial products such as heating, ventilation, and air conditioning (“HVAC”) systems. These products help improve performance, for example, by making an automobile’s heating and air conditioning systems work more efficiently, thereby improving gas mileage. These products are also used in systems that address safety and environmental concerns, for example by improving the stability control of the vehicle and reducing vehicle emissions.

Our controls business is a manufacturer of a variety of control products used in industrial, aerospace, military, commercial, and residential markets. These products include motor and compressor protectors, circuit breakers, semiconductor burn-in test sockets, electronic HVAC controls, power inverters, precision switches, and thermostats. These products help prevent damage from overheating and fires in a wide variety of applications, including commercial HVAC systems, refrigerators, aircraft, automobiles, lighting, and other industrial applications. The controls business also manufactures direct current to alternating current power inverters, which enable the operation of electronic equipment when grid power is not available.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (“U.S. GAAP”) for interim financial information and with the instructions to Form 10-Q, and therefore do not include all of the information and note disclosures required by U.S. GAAP for complete financial statements. The accompanying financial information reflects all normal recurring adjustments which are, in the opinion of management, necessary for a fair presentation of the interim period results. The results of operations for the three and six months ended June 30, 2014 are not necessarily indicative of the results to be expected for the full year, nor were those of the comparable 2013 periods necessarily representative of those actually experienced for the full year 2013. These unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2013.

All intercompany balances and transactions have been eliminated.

All U.S. dollar and share amounts presented, except per share amounts, are stated in thousands, unless otherwise indicated.

Certain reclassifications have been made to prior periods to conform to current period presentation.

2. New Accounting Standards

In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update (“ASU”) No. 2014-09, Revenue from Contracts with Customers (Topic 606) (“ASU 2014-09”), which modifies how all entities recognize revenue, and consolidates into one Accounting Standards Codification ("ASC") Topic (ASC Topic 606, Revenue from Contracts with Customers) the current guidance found in ASC Topic 605, Revenue Recognition, and various other revenue accounting standards for specialized transactions and industries. The core principle of the guidance is that “an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.” In achieving this objective, an entity must perform five steps: (1) identify the contract(s) with a customer, (2) identify the performance obligations of the contract, (3) determine the transaction price, (4) allocate the transaction price to the performance obligations in the contract, and (5) recognize revenue

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when (or as) the entity satisfies a performance obligation. ASU 2014-09 also clarifies how an entity should account for costs of obtaining or fulfilling a contract in a new ASC Subtopic 340-40, Other Assets and Deferred Costs - Contracts with Customers.

ASU 2014-09 is effective for public companies for annual periods beginning after December 15, 2016 and interim periods within those annual periods, and early adoption is not permitted. ASU 2014-09 may be applied using either a full retrospective approach, in which all years included in the financial statements are presented under the revised guidance, or a modified retrospective approach. Under the modified retrospective approach, financial statements will be prepared using the new standard for the year of adoption, but not for prior years. Under this method, entities will recognize a cumulative catch-up adjustment to the opening balance of retained earnings at the effective date for contracts that still require performance by the company and disclose all line items in the year of adoption as if they were prepared under the old revenue guidance. We will adopt ASU 2014-09 on January 1, 2017 and are currently evaluating the impact that this adoption will have on our consolidated financial statements. At this time, we have not determined the transition method that will be used.

3. Inventories

The components of inventories as of June 30, 2014 and December 31, 2013 were as follows:

	June 30, 2014	December 31, 2013
Finished goods	$86,513	$82,350
Work-in-process	40,974	32,790
Raw materials	98,571	68,255
Total	$226,058	$183,395

4. Shareholders' Equity

Treasury Shares

In October 2012, our Board of Directors authorized a $250.0 million share repurchase program. On October 28, 2013, the Board of Directors amended the terms of the share buyback program, resetting the amount available for share repurchases to $250.0 million. On February 3, 2014, our Board of Directors again amended the terms of our share buyback program, resetting the amount available for share repurchase to $250.0 million. Under the current amended program, we may repurchase ordinary shares from time to time, at such times and in amounts to be determined by our management, based on market conditions, legal requirements, and other corporate considerations, in the open market or in privately negotiated transactions. The current amended share repurchase program may be modified or terminated by our Board of Directors at any time.

During the six months ended June 30, 2014, we repurchased 4,291 ordinary shares for an aggregate purchase price of approximately $181.1 million at a weighted-average price of $42.21 per ordinary share. Of the ordinary shares repurchased, 4,000 were repurchased from Sensata Investment Company S.C.A. ("SCA") in a private, non-underwritten transaction, concurrent with the closing of the May 2014 secondary offering, at $42.42 per ordinary share, which was equal to the price paid by the underwriters.

During the six months ended June 30, 2013, we repurchased 3,877 ordinary shares for an aggregate purchase price of approximately $125.2 million at a weighted-average price of $32.30 per ordinary share.

Ordinary shares repurchased by us are recorded at cost as treasury shares and result in a reduction of shareholders' equity. We reissue treasury shares as part of our share-based compensation programs and employee stock purchase plan. When shares are reissued, we determine the cost using the first-in, first-out method. During the six months ended June 30, 2014 and June 30, 2013, we reissued 678 and 1,210 treasury shares, respectively, as part of our share-based compensation programs and employee stock purchase plan. During the six months ended June 30, 2014, in connection with our treasury share reissuances, we recognized a loss of $11.1 million that was recorded in Accumulated deficit.

Secondary Offering

In May 2014, we completed a secondary offering of our ordinary shares in which one of our existing shareholders, SCA, sold 11.5 million ordinary shares at an offering price of $42.42 per ordinary share. We did not receive any proceeds from this offering. As of June 30, 2014, SCA owned approximately 8.9% of our outstanding ordinary shares.

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Accumulated Other Comprehensive Loss

The following is a roll forward of the components of Accumulated other comprehensive loss, net of tax, for the six months ended June 30, 2014:

	Derivative Instruments Designated and Qualifying as Cash Flow Hedges	Defined Benefit and Retiree Healthcare Plans	Accumulated Other Comprehensive Loss
Balance as of December 31, 2013	$(7,612)	$(25,495)	$(33,107)
Other comprehensive income before reclassifications	183	—	183
Amounts reclassified from Accumulated other comprehensive loss	3,870	(200)	3,670
Net current period other comprehensive income/(loss)	4,053	(200)	3,853
Balance as of June 30, 2014	$(3,559)	$(25,695)	$(29,254)

The details of the amounts reclassified from Accumulated other comprehensive loss for the three and six months ended June 30, 2014 and June 30, 2013 are as follows:

For the three months ended June 30, 2014 and June 30, 2013

Component	Amount of Loss/(Gain) Reclassified from Accumulated Other Comprehensive Loss		Affected Line in Condensed Consolidated Statement of Operations
	For the three months ended June 30, 2014	For the three months ended June 30, 2013	
Derivative instruments designated and qualifying as cash flow hedges			
Interest rate caps	$415	$208	Interest expense [(1)]
Interest rate caps	—	1,097	Other, net [(1)]
Foreign currency forward contracts	2,797	(922)	Net revenue [(1)]
Foreign currency forward contracts	(217)	(658)	Cost of revenue [(1)]
	2,995	(275)	Total before tax
	(750)	69	Provision for income taxes
	$2,245	$(206)	Net of tax
Defined benefit and retiree healthcare plans	$(103)	$448	Various [(2)]
	(26)	(30)	Provision for income taxes
	$(129)	$418	Net of tax

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For the six months ended June 30, 2014 and June 30, 2013

Component	Amount of Loss/(Gain) Reclassified from Accumulated Other Comprehensive Loss		Affected Line in Condensed Consolidated Statement of Operations
	For the six months ended June 30, 2014	For the six months ended June 30, 2013	
Derivative instruments designated and qualifying as cash flow hedges			
Interest rate caps	$740	$515	Interest expense [1]
Interest rate caps	—	1,097	Other, net [1]
Foreign currency forward contracts	4,721	288	Net revenue [1]
Foreign currency forward contracts	(299)	(1,065)	Cost of revenue [1]
	5,162	835	Total before tax
	(1,292)	(209)	Provision for income taxes
	$3,870	$626	Net of tax
Defined benefit and retiree healthcare plans	$(186)	$930	Various [2]
	(14)	(58)	Provision for income taxes
	$(200)	$872	Net of tax

[1] See Note 12, "Derivative Instruments and Hedging Activities," for additional details on amounts to be reclassified in the future from Accumulated other comprehensive loss.

[2] Amounts related to defined benefit and retiree healthcare plans reclassified from Accumulated other comprehensive loss affect the Cost of revenue, Research and development, and Selling, general and administrative line items in the condensed consolidated statement of operations. These amounts reclassified are included in the computation of net periodic benefit cost. See Note 8, "Pension and Other Post-Retirement Benefits," for additional details of net periodic benefit cost.

5. Restructuring and Special Charges

Restructuring

Our restructuring programs are described below.

2011 Plan

In 2011, we committed to a restructuring plan (the "2011 Plan") to reduce the workforce in several business centers and manufacturing facilities throughout the world and to move certain manufacturing operations to our low-cost sites. In 2012, we expanded the 2011 Plan to include additional costs associated with ceasing manufacturing in our JinCheon, South Korea facility. These actions were completed in 2013, and we do not expect to incur any additional charges related to this plan.

MSP Plan

On January 28, 2011, we acquired the Magnetic Speed and Position business ("MSP") from Honeywell International Inc. On January 31, 2011, we announced a plan (the “MSP Plan”) to close the manufacturing facilities in Freeport, Illinois and Brno, Czech Republic. Restructuring charges related to these actions consisted primarily of severance and facility exit and other costs. These actions were completed in 2013, and we do not expect to incur any additional charges related to this plan. Substantially all remaining payments have been made.

Special Charges

On September 30, 2012, a fire damaged a portion of our manufacturing facility in JinCheon, South Korea. During the three months ended June 30, 2014, we recognized $4.9 million of insurance proceeds related to this fire, which were largely offset by

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certain charges and expenses incurred during the three months ended June 30, 2014 related to the completed transformation of our South Korean operations. During the six months ended June 30, 2014, we recognized a total of $7.3 million of insurance proceeds related to this fire. The insurance proceeds received during the three and six months ended June 30, 2014, and the offsetting charges and expenses incurred during the three months ended June 30, 2014, were recognized in the Cost of revenue line of our condensed consolidated statements of operations. During the six months ended June 30, 2013, we recognized $2.5 million of insurance proceeds related to this fire, of which $0.8 million was recorded in Restructuring and special charges, and the remainder in Cost of revenue. We did not recognize any insurance proceeds related to this fire during the three months ended June 30, 2013. As discussed in Note 10, "Commitments and Contingencies," we classify insurance proceeds in our condensed consolidated statements of operations in a manner consistent with the related losses.

Summary of Restructuring Programs

The following tables present costs/(gains) recorded within the condensed consolidated statements of operations associated with our restructuring activities and special charges, and where these amounts were recognized, for the three and six months ended June 30, 2014 and June 30, 2013:

	For the three months ended June 30, 2014				
	2011 Plan	MSP Plan	Other	Special Charges	Total
Restructuring and special charges	$(68)	$—	$1,808	$—	$1,740
Other, net	(3)	—	—	—	(3)
Cost of revenue	—	—	—	(1,655)	(1,655)
Total	$(71)	$—	$1,808	$(1,655)	$82

	For the three months ended June 30, 2013				
	2011 Plan	MSP Plan	Other	Special Charges	Total
Restructuring and special charges	$1,581	$—	$769	$—	$2,350
Other, net	(17)	—	3	—	(14)
Cost of revenue					