

WESTERN DIGITAL CORP
Form 10-Q
February 10, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended January 1, 2016

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: 1-8703

WESTERN DIGITAL CORPORATION
(Exact Name of Registrant as Specified in Its Charter)

Delaware 33-0956711
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

3355 Michelson Drive, Suite 100 92612
Irvine, California
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (949) 672-7000

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. 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 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

As of the close of business on February 8, 2016, 232,770,151 shares of common stock, par value \$.01 per share, were outstanding.

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Unless otherwise indicated, references herein to specific years and quarters are to our fiscal years and fiscal quarters, and references to financial information are on a consolidated basis. As used herein, the terms “we,” “us,” “our,” the “Company,” “WDC” and “Western Digital” refer to Western Digital Corporation and its subsidiaries, unless, we state, or the context indicates, otherwise.

WDC, a Delaware corporation, is the parent company of our data storage business. Our principal executive offices are located at 3355 Michelson Drive, Suite 100, Irvine, California 92612. Our telephone number is (949) 672-7000 and our website is www.westerndigital.com. The information on our website is not incorporated in this Quarterly Report on Form 10-Q.

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PART I. FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS

WESTERN DIGITAL CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS

(in millions, except par values; unaudited)

	January 1, 2016	July 3, 2015
ASSETS		
Current assets:		
Cash and cash equivalents	\$5,363	\$5,024
Short-term investments	497	262
Accounts receivable, net	1,650	1,532
Inventories	1,238	1,368
Other current assets	200	331
Total current assets	8,948	8,517
Property, plant and equipment, net	2,801	2,965
Goodwill	2,766	2,766
Other intangible assets, net	292	332
Other non-current assets	659	601
Total assets	\$15,466	\$15,181
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$1,806	\$1,881
Accrued expenses	505	470
Accrued compensation	315	330
Accrued warranty	144	150
Accrued arbitration award	32	—
Revolving credit facility	255	255
Current portion of long-term debt	188	156
Total current liabilities	3,245	3,242
Long-term debt	2,062	2,156
Other liabilities	602	564
Total liabilities	5,909	5,962
Commitments and contingencies (Notes 4, 5, and 6)		
Shareholders' equity:		
Preferred stock, \$.01 par value; authorized — 5 shares; issued and outstanding — none	—	—
Common stock, \$.01 par value; authorized — 450 shares; issued — 261 shares; outstanding — 232 and 230 shares, respectively	3	3
Additional paid-in capital	2,421	2,428
Accumulated other comprehensive loss	(8	) (20
Retained earnings	9,407	9,107
Treasury stock — common shares at cost; 29 and 31 shares, respectively	(2,266	) (2,299
Total shareholders' equity	9,557	9,219
Total liabilities and shareholders' equity	\$15,466	\$15,181

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

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WESTERN DIGITAL CORPORATION
 CONDENSED CONSOLIDATED STATEMENTS OF INCOME
 (in millions, except per share amounts; unaudited)

	Three Months Ended		Six Months Ended	
	January 1, 2016	January 2, 2015	January 1, 2016	January 2, 2015
Revenue, net	\$3,317	\$3,888	\$6,677	\$7,831
Cost of revenue	2,411	2,778	4,816	5,572
Gross profit	906	1,110	1,861	2,259
Operating expenses:				
Research and development	389	426	774	863
Selling, general and administrative	207	164	399	384
Charges related to arbitration award	32	1	32	15
Employee termination, asset impairment and other charges	27	53	83	62
Total operating expenses	655	644	1,288	1,324
Operating income	251	466	573	935
Other income (expense):				
Interest and other income	6	4	11	8
Interest and other expense	(13)	(12)	(26)	(25)
Total other expense, net	(7)	(8)	(15)	(17)
Income before income taxes	244	458	558	918
Income tax expense (benefit)	(7)	20	24	57
Net income	\$251	\$438	\$534	\$861
Income per common share:				
Basic	\$1.08	\$1.88	\$2.31	\$3.70
Diluted	\$1.07	\$1.84	\$2.28	\$3.60
Weighted average shares outstanding:				
Basic	232	233	231	233
Diluted	234	238	234	239
Cash dividends declared per share	\$0.50	\$0.40	\$1.00	\$0.80

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

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WESTERN DIGITAL CORPORATION
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
 (in millions; unaudited)

	Three Months Ended		Six Months Ended	
	January 1, 2016	January 2, 2015	January 1, 2016	January 2, 2015
Net income	\$251	\$438	\$534	\$861
Other comprehensive income (loss), net of tax:				
Net unrealized gain (loss) on foreign exchange contracts	38	(18	) 13	(44
Net unrealized loss on available-for-sale securities	(2	) —	(1) —
Other comprehensive income (loss), net of tax	36	(18	) 12	(44
Total comprehensive income	\$287	\$420	\$546	\$817

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

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WESTERN DIGITAL CORPORATION
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (in millions; unaudited)

	Six Months Ended	
	January 1, 2016	January 2, 2015
Operating Activities		
Net income	\$534	\$861
Adjustments to reconcile net income to net cash provided by operations:		
Depreciation and amortization	488	579
Stock-based compensation	79	80
Deferred income taxes	15	31
Gain from insurance recovery	—	(37)
Loss on disposal of assets	6	12
Non-cash portion of employee termination, asset impairment and other charges	18	19
Changes in:		
Accounts receivable, net	(118)	) 109
Inventories	127	(56)
Accounts payable	(58)	) 94
Accrued arbitration award	32	(758)
Accrued expenses	35	70
Accrued compensation	(15)	) (9)
Other assets and liabilities, net	—	75
Net cash provided by operating activities	1,143	1,070
Investing Activities		
Purchases of property, plant and equipment	(300)	) (306)
Proceeds from sale of property, plant and equipment	—	7
Proceeds from sales and maturities of investments	266	630
Purchases of investments	(408)	) (595)
Acquisitions, net of cash acquired	—	(6)
Other investing activities, net	(12)	) 16
Net cash used in investing activities	(454)	) (254)
Financing Activities		
Issuance of stock under employee stock plans	54	112
Taxes paid on vested stock awards under employee stock plans	(44)	) (59)
Excess tax benefits from employee stock plans	(6)	) 11
Repurchases of common stock	(60)	) (532)
Dividends paid to shareholders	(231)	) (187)
Repayment of debt	(63)	) (63)
Net cash used in financing activities	(350)	) (718)
Net increase in cash and cash equivalents	339	98
Cash and cash equivalents, beginning of period	5,024	4,804
Cash and cash equivalents, end of period	\$5,363	\$4,902
Supplemental disclosure of cash flow information:		
Cash paid (received) for income taxes	\$21	\$(45)
Cash paid for interest	\$22	\$23
Supplemental disclosure of non-cash financing activities:		
Accrual of cash dividend declared	\$116	\$93

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

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WESTERN DIGITAL CORPORATION
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
 (unaudited)

1. Basis of Presentation

The accounting policies followed by Western Digital Corporation (the “Company”) are set forth in Part II, Item 8, Note 1 of the Notes to Consolidated Financial Statements included in the Company’s Annual Report on Form 10-K for the year ended July 3, 2015. In the opinion of management, all adjustments necessary to fairly state the unaudited condensed consolidated financial statements have been made. All such adjustments are of a normal, recurring nature. Certain information and footnote disclosures normally included in the consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States (“U.S. GAAP”) have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). These unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto included in the Company’s Annual Report on Form 10-K for the year ended July 3, 2015. The results of operations for interim periods are not necessarily indicative of results to be expected for the full year. The Company’s fiscal year ends on the Friday nearest to June 30 and typically consists of 52 weeks. Approximately every six years, the Company reports a 53-week fiscal year to align its fiscal year with the foregoing policy. The Company’s fiscal second quarters ended January 1, 2016 and January 2, 2015 both consisted of 13 weeks. The six months ended January 1, 2016 and January 2, 2015 consisted of 26 and 27 weeks, respectively. Fiscal 2016 will be comprised of 52 weeks and will end on July 1, 2016. Fiscal year 2015 was comprised of 53 weeks and ended on July 3, 2015.

Company management has made estimates and assumptions relating to the reporting of certain assets and liabilities in conformity with U.S. GAAP. These estimates and assumptions have been applied using methodologies that are consistent throughout the periods presented. However, actual results could differ materially from these estimates.

2. Supplemental Financial Statement Data

Accounts Receivable

From time to time, in connection with a factoring agreement, the Company sells trade accounts receivable without recourse to a third party purchaser in exchange for cash. The Company did not sell trade accounts receivable during the three months ended January 1, 2016. During the six months ended January 1, 2016, the Company sold trade accounts receivable and received cash proceeds of \$200 million. The Company did not sell trade accounts receivable during the three and six months ended January 2, 2015. The discounts on the sales of trade accounts receivable were not material and were recorded within interest and other expense in the condensed consolidated statements of income.

Inventories; Property, Plant and Equipment; and Other Intangible Assets

	January 1, 2016 (in millions)	July 3, 2015
Inventories:		
Raw materials and component parts	\$ 130	\$ 168
Work-in-process	474	500
Finished goods	634	700