

MCGRATH RENTCORP
Form 10-Q
August 02, 2016

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, 2016

Commission file number 0-13292

MCGRATH RENTCORP

(Exact name of registrant as specified in its Charter)

California 94-2579843
(State or other jurisdiction (I.R.S. Employer

of incorporation or organization) Identification No.)
5700 Las Positas Road, Livermore, CA 94551-7800

(Address of principal executive offices)

Registrant's telephone number: (925) 606-9200

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

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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 definition 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 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 August 1, 2016, 23,907,760 shares of Registrant’s Common Stock were outstanding.

FORWARD LOOKING STATEMENTS

Statements contained in this Quarterly Report on Form 10-Q (this “Form 10-Q”) which are not historical facts are forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. All statements, other than statements of historical facts, regarding McGrath RentCorp’s (the “Company’s”) business strategy, future operations, financial position, estimated revenues or losses, projected costs, prospects, plans and objectives are forward-looking statements. These forward-looking statements appear in a number of places and can be identified by the use of forward-looking terminology such as “may,” “will,” “should,” “expect,” “plan,” “anticipate,” “believe,” “estimate,” “predict,” “future,” “intend,” “hopes” or “certain” or the negative of these terms or other variations or comparable terminology.

Management cautions that forward-looking statements are not guarantees of future performance and are subject to risks and uncertainties that could cause our actual results to differ materially from those projected in such forward-looking statements. Further, our future business, financial condition and results of operations could differ materially from those anticipated by such forward-looking statements and are subject to risks and uncertainties as set forth under “Risk Factors” in this form 10-Q.

Forward-looking statements are made only as of the date of this Form 10-Q and are based on management’s reasonable assumptions, however these assumptions can be wrong or affected by known or unknown risks and uncertainties. No forward-looking statement can be guaranteed and subsequent facts or circumstances may contradict, obviate, undermine or otherwise fail to support or substantiate such statements. Readers should not place undue reliance on these forward-looking statements and are cautioned that any such forward-looking statements are not guarantees of future performance. Except as otherwise required by law, we are under no duty to update any of the forward-looking statements after the date of this Form 10-Q to conform such statements to actual results or to changes in our expectations.

Part I - Financial Information

Item 1. Financial Statements

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders

McGrath RentCorp

We have reviewed the accompanying condensed consolidated balance sheet of McGrath RentCorp and subsidiaries (the "Company") as of June 30, 2016, and the related condensed consolidated statements of income and comprehensive income for the three-month and six-month periods ended June 30, 2016 and 2015, and cash flows for the six-month period ended June 30, 2016 and 2015. These interim financial statements are the responsibility of the Company's management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the condensed consolidated interim financial statements referred to above for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of the Company as of December 31, 2015, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for the year then ended (not presented herein); and we expressed an unqualified opinion on those consolidated financial statements in our report dated February 25, 2016. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2015, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ GRANT THORNTON LLP

San Jose, California

August 2, 2016

McGRATH RENTCORP

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(UNAUDITED)

(in thousands, except per share amounts)	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Revenues				
Rental	\$ 66,747	\$ 67,305	\$ 133,279	\$ 132,807
Rental related services	19,315	17,227	36,906	32,594
Rental operations	86,062	84,532	170,185	165,401
Sales	16,396	10,968	25,430	19,755
Other	647	526	1,189	1,058
Total revenues	103,105	96,026	196,804	186,214
Costs and Expenses				
Direct costs of rental operations:				
Depreciation of rental equipment	18,231	19,016	36,771	37,698
Rental related services	13,984	12,901	27,164	24,800
Other	16,713	16,226	32,540	31,437
Total direct costs of rental operations	48,928	48,143	96,475	93,935
Costs of sales	10,421	6,965	15,918	12,274
Total costs of revenues	59,349	55,108	112,393	106,209
Gross profit	43,756	40,918	84,411	80,005
Selling and administrative expenses	25,683	24,453	52,080	49,665
Income from operations	18,073	16,465	32,331	30,340
Other income (expense):				
Interest expense	(2,990)	(2,347)	(6,546)	(4,738)
Foreign currency exchange gain (loss)	(77)	(85)	74	(253)
Income before provision for income taxes	15,006	14,033	25,859	25,349
Provision for income taxes	5,927	5,543	10,214	10,013
Net income	\$ 9,079	\$ 8,490	\$ 15,645	\$ 15,336
Earnings per share:				
Basic	\$ 0.38	\$ 0.33	\$ 0.66	\$ 0.59
Diluted	\$ 0.38	\$ 0.32	\$ 0.65	\$ 0.58
Shares used in per share calculation:				
Basic	23,900	26,142	23,881	26,117
Diluted	23,949	26,273	23,931	26,272
Cash dividends declared per share	\$ 0.255	\$ 0.250	\$ 0.510	\$ 0.500

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

McGRATH RENTCORP

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(UNAUDITED)

(in thousands)	Three Months Ended June		Six Months Ended June	
	30, 2016	2015	30, 2016	2015
Net income	\$ 9,079	\$ 8,490	\$ 15,645	\$ 15,336
Other comprehensive income (loss):				
Foreign currency translation adjustment	5	6	(87)	89
Tax benefit (provision)	(1)	—	33	(16)
Comprehensive income	\$ 9,083	\$ 8,496	\$ 15,591	\$ 15,409

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

McGrath RentCorp

CONDENSED CONSOLIDATED BALANCE SHEETS

(unaudited)

(in thousands)	June 30, 2016	December 31, 2015
Assets		
Cash	\$ 1,238	\$ 1,103
Accounts receivable, net of allowance for doubtful accounts of \$2,087 in 2016 and 2015	95,860	95,263
Income taxes receivable	—	11,000
Rental equipment, at cost:		
Relocatable modular buildings	761,125	736,875
Electronic test equipment	251,080	262,945
Liquid and solid containment tanks and boxes	310,089	310,263
	1,322,294	1,310,083
Less accumulated depreciation	(453,872)	(440,482)
Rental equipment, net	868,422	869,601
Property, plant and equipment, net	114,241	109,753
Prepaid expenses and other assets	31,419	28,556
Intangible assets, net	9,030	9,465
Goodwill	27,808	27,808
Total assets	\$ 1,148,018	\$ 1,152,549
Liabilities and Shareholders' Equity		
Liabilities:		
Notes payable	\$ 363,121	\$ 381,281
Accounts payable and accrued liabilities	73,779	71,942
Deferred income	38,349	36,288
Deferred income taxes, net	289,456	283,351
Total liabilities	764,705	772,862
Shareholders' equity:		
Common stock, no par value - Authorized 40,000 shares Issued and outstanding - 23,907 shares as of June 30, 2016 and 23,851 shares as of December 31, 2015	101,313	101,046
Retained earnings	282,121	278,708
Accumulated other comprehensive loss	(121)	(67)
Total shareholders' equity	383,313	379,687
Total liabilities and shareholders' equity	\$ 1,148,018	\$ 1,152,549

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

McGrath RentCorp

CONDENSED Consolidated Statements of Cash Flows

(unaudited)

(in thousands)	Six Months Ended	
	June 30, 2016	2015
Cash Flows from Operating Activities :		
Net income	\$15,645	\$15,336
Adjustments to reconcile net income to net cash provided by		
operating activities:		
Depreciation and amortization	41,417	42,171
Provision for doubtful accounts	987	690
Share-based compensation	1,586	1,953
Gain on sale of used rental equipment	(6,282)	(5,565)
Foreign currency exchange loss (gain)	(74)	253
Change in:		
Accounts receivable	(1,584)	6,630
Income taxes receivable	11,000	—
Prepaid expenses and other assets	(2,863)	7,981
Accounts payable and accrued liabilities	5,232	1,715
Deferred income	2,061	587
Deferred income taxes	6,105	(6,514)
Net cash provided by operating activities	73,230	65,237
Cash Flows from Investing Activities:		
Purchase of rental equipment	(45,715)	(71,237)
Purchase of property, plant and equipment	(8,698)	(5,832)
Proceeds from sale of used rental equipment	13,059	11,815
Net cash used in investing activities	(41,354)	(65,254)
Cash Flows from Financing Activities:		
Net borrowings under bank lines of credit	1,814	34,699
Principal payments on Series A senior notes	(20,000)	(20,000)
Amortization of debt issuance costs	26	26
Proceeds from the exercise of stock options	37	1,458
Excess tax benefit (shortfall) from exercise of stock awards	(871)	313
Taxes paid related to net share settlement of stock awards	(486)	(584)
Repurchase of common stock	—	(3,132)
Payment of dividends	(12,253)	(13,176)
Net cash used in financing activities	(31,733)	(396)
Effect of exchange rate changes on cash	(8)	(15)
Net increase (decrease) in cash	135	(428)
Cash balance, beginning of period	1,103	1,167
Cash balance, end of period	\$1,238	\$739
Supplemental Disclosure of Cash Flow Information:		

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Interest paid, during the period	\$6,646	\$4,896
Net income taxes paid, during the period	\$5,679	\$1,490
Dividends accrued during the period, not yet paid	\$6,135	\$6,588
Rental equipment acquisitions, not yet paid	\$3,935	\$8,390

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

McGRATH RENTCORP

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2016

NOTE 1. CONDENSED CONSOLIDATED FINANCIAL INFORMATION

The condensed consolidated financial statements for the three and six months ended June 30, 2016 and 2015 have not been audited, but in the opinion of management, all adjustments (consisting of normal recurring accruals, consolidating and eliminating entries) necessary for the fair presentation of the consolidated financial position, results of operations and cash flows of McGrath RentCorp (the “Company”) have been made. The accompanying unaudited condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”). Certain information and note disclosures normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) have been condensed or omitted pursuant to those rules and regulations. The consolidated results for the six months ended June 30, 2016 should not be considered as necessarily indicative of the consolidated results for the entire fiscal year. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s latest Annual Report on Form 10-K filed with the SEC on February 25, 2016 for the year ended December 31, 2015 (the “2015 Annual Report”).

NOTE 2. NEW ACCOUNTING PRONOUNCEMENTS

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2014-09, Revenue from Contracts with Customers. The objective of this guidance is to establish the principles to report useful information to users of financial statements about the nature, timing and uncertainty of revenue from contracts with customers. In August 2015, the FASB issued an update to defer the effective date of this guidance by one year. The guidance in the update is effective for the interim and annual reporting periods beginning after December 15, 2017. The Company is evaluating the impact of the adoption of this accounting guidance on its consolidated financial statements.

In April 2015, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2015-03, Imputation of Interest (Subtopic 835-30). The amendments in this update require that debt issuance costs related to a recognized debt liability be presented on the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with the presentation of debt discounts. The implementation of this update resulted in a reclassification of \$0.2 million of debt issuance costs from prepaid expenses and other assets to notes payable at December 31, 2015.

In February 2016, the FASB issued ASU No. 2016-02, Leases (Subtopic 842-10). Under the new guidance, lessees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date: a) lease liability, which is a lessee’s obligation to make lease payments arising from a lease,

measured on a discounted basis; and b) right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Under the new guidance, lessor accounting is largely unchanged. The amendments are effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. The Company is evaluating the impact of the adoption of this guidance on its consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09, Compensation – Stock Compensation (Topic 718). Under the new guidance, all excess tax benefits and tax deficiencies will be recognized in the income statement as they occur. This will replace the current guidance, which requires tax benefits that exceed compensation cost (windfalls) to be recognized in equity. It will also eliminate the need to maintain a “windfall pool,” and will remove the requirement to delay recognizing a windfall until it reduces current taxes payable. The new guidance will also change the cash flow presentation of excess tax benefits, classifying them as operating inflows, consistent with other cash flows related to income taxes. The amendments in this guidance are effective for fiscal years beginning after December 15, 2016 and interim periods within those fiscal years. The Company is evaluating the impact of the adoption of this new guidance on its consolidated financial statements.

In April 2016, the FASB issued ASU No. 2016-10, Revenue from Contract with Customers (Topic 606): Identifying Performance Obligations and Licensing. The amendments clarify the following two aspects of Topic 606: (a) identifying performance obligations; and (b) the licensing implementation guidance. The amendments do not change the core principle of the guidance in Topic 606. The amendments are effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. The Company is evaluating the impact of the adoption of this guidance on its consolidated financial statements.

In May 2016, the FASB issued ASU No. 2016-12, Revenue from Contract with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedient. The amendments do not change the core revenue recognition principle in Topic 606. The amendments provide clarifying guidance in certain narrow areas and add some practical expedient. The amendments are effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. The Company is evaluating the impact of the adoption of this guidance on its consolidated financial statements.

NOTE 3. EARNINGS PER SHARE

Basic earnings per share (“EPS”) is computed as net income divided by the weighted-average number of shares of common stock outstanding for the period. Diluted EPS is computed assuming conversion of all potentially dilutive securities including the dilutive effect of stock options, unvested restricted stock awards and other potentially dilutive securities. The table below presents the weighted-average number of shares of common stock used to calculate basic and diluted earnings per share:

	Three Months Ended		Six Months Ended	
(in thousands)	June 30, 2016	2015	June 30, 2016	2015
Weighted-average number of shares of common stock for				
calculating basic earnings per share	23,900	26,142	23,881	26,117
Effect of potentially dilutive securities from				
equity-based compensation	49	131	50	155
Weighted-average number of shares of common stock for				
calculating diluted earnings per share	23,949	26,273	23,931	26,272

The following securities were not included in the computation of diluted earnings per share as their effect would have been anti-dilutive:

	Three Months Ended		Six Months Ended	
(in thousands)	June 30, 2016	2015	June 30, 2016	2015

Options to purchase shares of common stock 989 650 989 215

In May 2008, the Company's Board of Directors authorized the Company to repurchase an aggregate of 2,000,000 shares of the Company's outstanding common stock. The Company has in the past made purchases of shares of its common stock from time to time in over-the-counter market (NASDAQ) transactions, through privately negotiated, large block transactions and through a share repurchase plan, in accordance with Rule 10b5-1 of the Securities Exchange Act of 1934. In August 2015, the Company's Board of Directors authorized the Company to repurchase an additional 2,000,000 shares of the Company's outstanding common stock. The amount and time of the specific repurchases are subject to prevailing market conditions, applicable legal requirements and other factors, including management's discretion. All shares repurchased by the Company are canceled and returned to the status of authorized but unissued shares of common stock. There can be no assurance that any shares authorized for repurchase will be repurchased and the repurchase program may be modified, extended or terminated by the Board of Directors at any time. The following table presents share repurchase activities during the three and six months ended June 30, 2016 and 2015.

	Three Months Ended	Six Months Ended
(in thousands, except share and per share amounts)	June 30, 2016	June 30, 2015
Number of shares repurchased	— 89	— 102
Aggregate purchase price	\$—\$2,754	\$—\$3,132
Average price per repurchased shares	\$—\$30.79	\$—\$30.81

As of June 30, 2016, 1,592,026 shares remain authorized for repurchase.

NOTE 4. 2016 STOCK INCENTIVE PLAN

The Company adopted the 2016 Stock Incentive Plan (the "2016 Plan"), effective June 8, 2016, under which 2,000,000 shares of common stock of the Company, plus the number of shares that remain available for grants of awards under the Company's 2007 Stock

Option Plan (the “2007 Plan”) and become available as a result of forfeiture, termination, or expiration of awards previously granted under the 2007 Plan, were reserved for the grant of equity awards to its employees, directors and consultants. The equity awards have a maximum term of 7 years at an exercise price of not less than 100% of the fair market value of the Company's common stock on the date the equity award is granted. The 2016 Plan replaces the Company’s 2007 Plan.

NOTE 5. INTANGIBLE ASSETS

Intangible assets consist of the following:

	Estimated		
	useful life	June 30,	December 31,
(dollar amounts in thousands)	in years	2016	2015
Trade name	Indefinite	\$5,700	\$ 5,700
Customer relationships	11	9,611	9,611
		15,311	15,311
Less accumulated amortization		(6,281)	(5,846)
		\$9,030	\$ 9,465

The Company assesses potential impairment of its goodwill and intangible assets when there is evidence that events or circumstances have occurred that would indicate the recovery of an asset’s carrying value is unlikely. The Company also assesses potential impairment of its goodwill and intangible assets on an annual basis regardless of whether there is evidence of impairment. If indicators of impairment were to be present in intangible assets used in operations and future discounted cash flows were not expected to be sufficient to recover the assets’ carrying amount, an impairment loss would be charged to expense in the period identified. The amount of an impairment loss that would be recognized is the excess of the asset’s carrying value over its fair value. Factors the Company considers important, which may cause impairment include, among others, significant changes in the manner of use of the acquired asset, negative industry or economic trends, and significant underperformance relative to historical or projected operating results.

The Company typically conducts its annual impairment analysis in the fourth quarter of its fiscal year. The impairment analysis did not result in an impairment charge for the fiscal year ended December 31, 2015. Determining the fair value of a reporting unit is judgmental and involves the use of significant estimates and assumptions. The Company bases its fair value estimates on assumptions that it believes are reasonable but are uncertain and subject to changes in market conditions.

Intangible assets with finite useful lives are amortized over their respective useful lives. Based on the carrying values at June 30, 2016 and assuming no subsequent impairment of the underlying assets, the amortization expense is expected to be \$0.5 million for the remainder of fiscal year 2016, \$0.9 million in each of the fiscal years 2017 through 2019 and \$0.2 million in 2020.

NOTE 6. SEGMENT REPORTING

The Company's four reportable segments are (1) its modular building and portable storage segment ("Mobile Modular"); (2) its electronic test equipment segment ("TRS-RenTelco"); (3) its containment solutions for the storage of hazardous and non-hazardous liquids and solids segment ("Adler Tanks"); and (4) its classroom manufacturing segment selling modular buildings used primarily as classrooms in California ("Enviroplex"). The operations of each of these segments are described in Part I – Item 1, "Business," and the accounting policies of the segments are described in "Note 2 – Significant Accounting Policies" in the Company's annual report on Form 10-K for the year ended December 31, 2015. Management focuses on several key measures to evaluate and assess each segment's performance, including rental revenue growth, gross profit, income from operations and income before provision for income taxes. Excluding interest expense, allocations of revenue and expense not directly associated with one of these segments are generally allocated to Mobile Modular, TRS-RenTelco and Adler Tanks based on their pro-rata share of direct revenues. Interest expense is allocated among Mobile Modular, TRS-RenTelco and Adler Tanks based on their pro-rata share of average rental equipment at cost, intangible assets, accounts receivable, deferred income and customer security deposits. The Company does not report total assets by business segment. Summarized financial information for the six months ended June 30, 2016 and 2015 for the Company's reportable segments is shown in the following table:

	Mobile Modular	TRS- RenTelco	Adler Tanks	Enviroplex ¹	Consolidated
(dollar amounts in thousands)					
Six Months Ended June 30,					
2016					
Rental revenues	\$62,792	\$41,197	\$29,290	\$ —	\$ 133,279
Rental related services revenues	23,337	1,501	12,068	—	36,906
Sales and other revenues	8,634	13,194	644	4,147	26,619
Total revenues	94,763	55,892	42,002	4,147	196,804
Depreciation of rental equipment	10,347	18,386	8,038	—	36,771
Gross profit	41,287	22,558	19,077	1,489	84,411
Selling and administrative expenses	24,798	11,343	14,155	1,784	52,080
Income (loss) from operations	16,489	11,215	4,922	(295)	32,331
Interest (expense) income allocation	(3,602)	(1,340)	(1,719)	115	(6,546)
Income (loss) before provision for income taxes	12,887	9,949	3,203	(180)	25,859
Rental equipment acquisitions	26,448	15,373	550	—	42,371
Accounts receivable, net (period end)	52,362	23,098	15,757	4,643	95,860
Rental equipment, at cost (period end)	761,125	251,080	310,089		1,322,294
Rental equipment, net book value (period end)	544,132	94,320	229,970		868,422
Utilization (period end) ²	75.7 %	59.7 %	46.8 %		
Average utilization ²	76.0 %	59.5 %	49.7 %		
2015					
Rental revenues	\$54,088	\$44,000	\$34,719	\$ —	\$ 132,807
Rental related services revenues	19,591	1,450	11,553	—	32,594
Sales and other revenues	7,325	10,545	742	2,201	20,813
Total revenues	81,004	55,995	47,014	2,201	186,214
Depreciation of rental equipment	9,280	20,477	7,941	—	37,698
Gross profit	32,266	22,751	24,380	608	80,005
Selling and administrative expenses	22,642	11,611	13,819	1,593	49,665
Income (loss) from operations	9,624	11,140	10,561	(985)	30,340

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Interest (expense) income allocation	(2,481)	(1,053)	(1,297)	93	(4,738)
Income (loss) before provision for income taxes	7,143	9,834	9,264	(892)	25,349
Rental equipment acquisitions	38,691	30,077	5,919	—	74,687
Accounts receivable, net (period end)	46,913	23,547	20,310	3,204	93,974
Rental equipment, at cost (period end)	699,781	269,668	307,795		1,277,244
Rental equipment, net book value (period end)	501,071	112,275	243,143		856,489
Utilization (period end) ²	74.3 %	60.3 %	61.7 %		
Average utilization ²	74.3 %	59.8 %	60.9 %		

1. Gross Enviroplex sales revenues were \$4,147 and \$2,208 for the six months ended June 30, 2016 and 2015, respectively, which include inter-segment sales to Mobile Modular of \$0 and \$7, respectively, which have been eliminated in consolidation.

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2. Utilization is calculated each month by dividing the cost of rental equipment on rent by the total cost of rental equipment excluding accessory equipment and for Mobile Modular and Adler Tanks excluding new equipment inventory. The Average Utilization for the period is calculated using the average costs of rental equipment. No single customer accounted for more than 10% of total revenues for the six months ended June 30, 2016 and 2015. Revenues from foreign country customers accounted for 5% and 6% of the Company's total revenues for the same periods, respectively.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

This Form 10-Q, including the following Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A"), contains forward-looking statements under federal securities laws. Forward-looking statements are not guarantees of future performance and involve a number of risks and uncertainties. Our actual results could differ materially from those indicated by forward-looking statements as a result of various factors. These factors include, but are not limited to, those set forth under this Item, those discussed in Part II—Item 1A, "Risk Factors" and elsewhere in this Form 10-Q and in our Annual Report on Form 10-K for the year ended December 31, 2015, as filed with the SEC on February 25, 2016 (the "2015 Annual Report") and those that may be identified from time to time in our reports and registration statements filed with the SEC.

This discussion should be read in conjunction with the Condensed Consolidated Financial Statements and related Notes included in Part I—Item 1 of this Form 10-Q and the Consolidated Financial Statements and related Notes and the Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our 2015 Annual Report. In preparing the following MD&A, we presume that readers have access to and have read the MD&A in our 2015 Annual Report, pursuant to Instruction 2 to paragraph (b) of Item 303 of Regulation S-K. We undertake no duty to update any of these forward-looking statements after the date of filing of this Form 10-Q to conform such forward-looking statements to actual results or revised expectations, except as otherwise required by law.

General

The Company, incorporated in 1979, is a leading rental provider of relocatable modular buildings for classroom and office space, electronic test equipment for general purpose and communications needs, and liquid and solid containment tanks and boxes. The Company's primary emphasis is on equipment rentals. The Company is comprised of four reportable business segments: (1) its modular building and portable storage container rental segment ("Mobile Modular"); (2) its electronic test equipment segment ("TRS-RenTelco"); (3) its containment solutions for the storage of hazardous and non-hazardous liquids and solids segment ("Adler Tanks"); and (4) its classroom manufacturing segment selling modular buildings used primarily as classrooms in California ("Enviroplex").

The Mobile Modular business segment includes the results of operations of Mobile Modular Portable Storage division, which represented approximately 7% of the Company's total revenues in the six months ended June 30, 2016. Mobile Modular Portable Storage offers portable storage units and high security portable office units for rent, lease and purchase.

In the six months ended June 30, 2016, Mobile Modular, TRS-RenTelco, Adler Tanks and Enviroplex contributed 50%, 39%, 12% and negative 1% of the Company's income before provision for taxes (the equivalent of "pretax income"), respectively, compared to 28%, 39%, 37% and negative 4% for the same period in 2015. Although managed as a separate business unit, Enviroplex's revenues, pretax income contribution and total assets are not significant relative to the Company's consolidated financial position. Accordingly, we have not presented a separate discussion of Enviroplex's results of operations in this MD&A.

The Company generates its revenues primarily from the rental of its equipment on operating leases and from sales of equipment occurring in the normal course of business. The Company requires significant capital outlay to purchase its rental inventory and recovers its investment through rental and sales revenues. Rental revenues and certain other service revenues negotiated as part of lease agreements with customers and related costs are recognized on a straight-line basis over the terms of the leases. Sales revenues and related costs are recognized upon delivery and installation of the equipment to customers. Sales revenues are less predictable and can fluctuate from quarter to quarter and year to year depending on customer demands and requirements. Generally, rental revenues less cash operating costs recover the equipment's capitalized cost in a shorter period of time relative to the equipment's potential

rental life and when sold, sale proceeds are usually above its net book value.

The Company's modular revenues (consisting of revenues from Mobile Modular, Mobile Modular Portable Storage and Enviroplex) are derived from rentals and sales to education and commercial customers, with a majority of revenues generated by education customers. Modular revenues are primarily affected by demand for classrooms, which in turn is affected by shifting and fluctuating school populations, the levels of state funding to public schools, the need for temporary classroom space during reconstruction of older schools and changes in policies regarding class size. As a result of any reduced funding, lower expenditures by these schools may result in certain planned programs to increase the number of classrooms, such as those that the Company provides, to be postponed or terminated. However, reduced expenditures may also result in schools reducing their long-term facility construction projects in favor of using the Company's modular classroom solutions. At this time, the Company can provide no assurances as to whether public schools will either reduce or increase their demand for the Company's modular classrooms as a result of fluctuations in state funding of public schools. Looking forward, the Company believes that any interruption in the passage of facility bonds or contraction of class size reduction programs by public schools may have a material adverse effect on both rental and sales revenues of the Company. (For more information, see "Item 1. Business – Relocatable Modular Buildings – Classroom Rentals and Sales to Public Schools (K-12)" in the Company's 2015 Annual Report and "Item 1A. Risk Factors – Significant reductions of, or delays in, funding to public schools have

caused the demand and pricing for our modular classroom units to decline, which has in the past caused, and may cause in the future, a reduction in our revenues and profitability” in Part II – Other Information of this Form 10-Q.)

Revenues of TRS-RenTelco are derived from the rental and sale of general purpose and communications test equipment to a broad range of companies, from Fortune 500 to middle and smaller market companies primarily in the aerospace, defense, communications, manufacturing and semiconductor industries. Electronic test equipment revenues are primarily affected by the business activity within these industries related to research and development, manufacturing, and communication infrastructure installation and maintenance.

Revenues of Adler Tanks are derived from the rental and sale of fixed axle tanks (“tanks”) and vacuum containers, dewatering containers and roll-off containers (collectively referred to as “boxes”). These tanks and boxes are rented to a broad range of industries and applications including oil and gas exploration and field services, refinery, chemical and industrial plant maintenance, environmental remediation and field services, infrastructure building construction, marine services, pipeline construction and maintenance, tank terminals services, wastewater treatment, and waste management and landfill services for the containment of hazardous and non-hazardous liquids and solids. The liquid and solid containment tanks and boxes rental business was acquired through the acquisition of Adler Tank Rentals, LLC on December 11, 2008.

The Company’s rental operations include rental and rental related service revenues which comprised approximately 86% and 89% of consolidated revenues in the six months ended June 30, 2016 and 2015, respectively. Of the total rental operations revenues for the six months ended June 30, 2016, Mobile Modular, TRS-RenTelco and Adler Tanks comprised 51%, 25% and 24%, respectively, compared to 45%, 27% and 28%, respectively, in the same period of 2015. The Company’s direct costs of rental operations include depreciation of rental equipment, rental related service costs, impairment of rental equipment (if any), and other direct costs of rental operations (which include direct labor, supplies, repairs, insurance, property taxes, license fees, cost of sub-rentals and amortization of certain lease costs).

The Company’s Mobile Modular, TRS-RenTelco and Adler Tanks business segments sell modular units, electronic test equipment and liquid and solid containment tanks and boxes, respectively, which are either new or previously rented. In addition, Enviroplex sells new modular buildings used primarily as classrooms in California. For the six months ended June 30, 2016 and 2015, sales and other revenues of modular, electronic test equipment and liquid and solid containment tanks and boxes comprised approximately 14% and 11% of the Company’s consolidated revenues, respectively. Of the total sales and other revenues for the six months ended June 30, 2016 and 2015, Mobile Modular and Enviroplex together comprised 48% and 46%, respectively, TRS-RenTelco comprised 50% and 51%, respectively, and Adler Tanks comprised 2% and 3%, respectively. The Company’s cost of sales includes the carrying value of the equipment sold and the direct costs associated with the equipment sold, such as delivery, installation, modifications and related site work.

Selling and administrative expenses primarily include personnel and benefit costs, which include share-based compensation, depreciation and amortization, bad debt expense, advertising costs, and professional service fees. The Company believes that sharing of common facilities, financing, senior management, and operating and accounting systems by all of the Company’s operations results in an efficient use of overhead. Historically, the Company’s operating margins have been impacted favorably to the extent its costs and expenses are leveraged over a large installed customer base. However, there can be no assurance as to the Company’s ability to maintain a large installed customer base or ability to sustain its historical operating margins.

Adjusted EBITDA

To supplement the Company’s financial data presented on a basis consistent with accounting principles generally accepted in the United States of America (“GAAP”), the Company presents “Adjusted EBITDA”, which is defined by the

Company as net income before interest expense, provision for income taxes, depreciation, amortization, and share-based compensation. The Company presents Adjusted EBITDA as a financial measure as management believes it provides useful information to investors regarding the Company's liquidity and financial condition and because management, as well as the Company's lenders, use this measure in evaluating the performance of the Company.

Management uses Adjusted EBITDA as a supplement to GAAP measures to further evaluate period-to-period operating performance, compliance with financial covenants in the Company's revolving lines of credit and senior notes and the Company's ability to meet future capital expenditure and working capital requirements. Management believes the exclusion of non-cash charges, including share-based compensation, is useful in measuring the Company's cash available for operations and performance of the Company. Because management finds Adjusted EBITDA useful, the Company believes its investors will also find Adjusted EBITDA useful in evaluating the Company's performance.

Adjusted EBITDA should not be considered in isolation or as a substitute for net income, cash flows, or other consolidated income or cash flow data prepared in accordance with GAAP or as a measure of the Company's profitability or liquidity. Adjusted EBITDA is not in accordance with or an alternative for GAAP, and may be different from non-GAAP measures used by other companies. Unlike EBITDA, which may be used by other companies or investors, Adjusted EBITDA does not include share-based compensation charges. The Company believes that Adjusted EBITDA is of limited use in that it does not reflect all of the amounts associated with the Company's results of operations as determined in accordance with GAAP and does not accurately reflect real cash flow. In addition, other companies may not use Adjusted EBITDA or may use other non-GAAP measures, limiting the usefulness of Adjusted EBITDA for purposes of comparison. The Company's presentation of Adjusted EBITDA should not be construed as an inference that the Company will not incur expenses that are the same as or similar to the adjustments in this presentation. Therefore, Adjusted EBITDA should only be used to evaluate the Company's results of operations in conjunction with the corresponding GAAP measures. The Company compensates for the limitations of Adjusted EBITDA by relying upon GAAP results to gain a complete picture of the Company's performance. Because Adjusted EBITDA is a non-GAAP financial measure, as defined by the SEC, the Company includes in the tables below reconciliations of Adjusted EBITDA to the most directly comparable financial measures calculated and presented in accordance with GAAP.

Reconciliation of Net Income to Adjusted EBITDA

	Three Months Ended		Six Months Ended		Twelve Months Ended	
	June 30, 2016	2015	June 30, 2016	2015	June 30, 2016	2015
(dollar amounts in thousands)						
Net income	\$9,079	\$8,490	\$15,645	\$15,336	\$40,779	\$42,969
Provision for income taxes	5,927	5,543	10,214	10,013	26,108	29,211
Interest	2,990	2,347	6,546	4,738	11,900	9,480
Depreciation and amortization	20,557	21,265	41,417	42,171	83,526	83,314
EBITDA	38,553	37,645	73,822	72,258	162,313	164,974
Share-based compensation	730	1,022	1,586	1,953	3,032	3,823
Adjusted EBITDA ¹	\$39,283	\$38,667	\$75,408	\$74,211	\$165,345	\$168,797
Adjusted EBITDA margin ²	38 %	40 %	38 %	40 %	40 %	41 %

Reconciliation of Adjusted EBITDA to Net Cash Provided by Operating Activities

	Three Months Ended		Six Months Ended		Twelve Months Ended	
	June 30, 2016	2015	June 30, 2016	2015	June 30, 2016	2015
(dollar amounts in thousands)						
Adjusted EBITDA ¹	\$39,283	\$38,667	\$75,408	\$74,211	\$165,345	\$168,797
Interest paid	(3,660)	(2,888)	(6,646)	(4,896)	(11,791)	(9,772)
Net income taxes paid	(4,973)	(1,174)	(5,679)	(1,490)	(6,687)	(15,239)

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Gain on sale of used rental equipment	(3,316)	(2,696)	(6,282)	(5,565)	(12,619)	(14,489)
Foreign currency exchange loss (gain)	77	65	(74)	253	161	574
Change in certain assets and liabilities:						
Accounts receivable, net	(3,977)	(4,613)	(597)	7,320	(1,886)	(4,890)
Income taxes receivable	—	—	11,000	—	—	—
Prepaid expenses and other assets	(4,812)	1,857	(2,863)	7,981	1,812	(3,410)
Accounts payable and other liabilities	13,451	1,032	6,902	(13,164)	9,535	7,811
Deferred income	1,525	367	2,061	587	8,623	3,643
Net cash provided by operating activities	\$33,598	\$30,617	\$73,230	\$65,237	\$152,493	\$133,025

- Adjusted EBITDA is defined as net income before interest expense, provision for income taxes, depreciation, amortization, and share-based compensation.
- Adjusted EBITDA margin is calculated as Adjusted EBITDA divided by total revenues for the period. Adjusted EBITDA is a component of two restrictive financial covenants for the Company's unsecured Credit Facility, and Series A Senior Notes, Series B Senior Notes and Series C Senior Notes (as defined and more fully described under the heading "Liquidity and Capital Resources" in this MD&A). These instruments contain financial covenants requiring the Company to not:
 - Permit the Consolidated Fixed Charge Coverage Ratio (as defined in the Credit Facility and the Note Purchase Agreement (as defined and more fully described under the heading "Liquidity and Capital Resources" in this MD&A)) of Adjusted

EBITDA (as defined in the Credit Facility and the Note Purchase Agreement) to fixed charges as of the end of any fiscal quarter to be less than 2.50 to 1. At June 30, 2016, the actual ratio was 3.79 to 1.

· Permit the Consolidated Leverage Ratio of funded debt (as defined in the Credit Facility and the Note Purchase Agreement) to Adjusted EBITDA at any time during any period of four consecutive quarters to be greater than 2.75 to 1. At June 30, 2016, the actual ratio was 2.20 to 1.

At June 30, 2016, the Company was in compliance with each of the aforementioned covenants. There are no anticipated trends that the Company is aware of that would indicate non-compliance with these covenants, although, significant deterioration in our financial performance could impact the Company's ability to comply with these covenants.

Recent Developments

On June 8, 2016, the Company announced that the Board of Directors declared a quarterly cash dividend of \$0.255 per common share for the quarter ended June 30, 2016, an increase of 2% over the prior year's comparable quarter.

Results of Operations

Three Months Ended June 30, 2016 Compared to

Three Months Ended June 30, 2015

Overview

Consolidated revenues for the three months ended June 30, 2016 increased 7% to \$103.1 million from \$96.0 million in the same period in 2015. Consolidated net income for the three months ended June 30, 2016 increased 7% to \$9.1 million, from \$8.5 million for the same period in 2015. Earnings per diluted share for the three months ended June 30, 2016 increased 19% to \$0.38 from \$0.32 for the same period in 2015.

For the three months ended June 30, 2016, on a consolidated basis:

- Gross profit increased \$2.8 million, or 7%, to \$43.8 million in 2016. Mobile Modular's gross profit increased \$4.1 million, or 25%, due to higher gross profit on rental, rental related services and sales revenues. Enviroplex's gross profit increased \$0.9 million, or 167%, primarily due to higher sales revenues. TRS-RenTelco's gross profit increased \$0.1 million, or 1%, primarily due to higher gross profit on sales revenues, partly offset by lower gross profit on rental revenues. Adler Tanks' gross profit decreased \$2.2 million, or 18%, primarily due to lower gross profit on rental revenues, partly offset by higher gross profit on rental related services and sales revenues.
- Selling and administrative expenses increased \$1.2 million, or 5%, to \$25.7 million, primarily due to increased employee headcount, salaries and employee benefit costs.
- Interest expense increased \$0.6 million, or 27%, to \$3.0 million in 2016 compared to the same period in 2015, due to 10% higher average debt levels of the Company and 16% higher net average interest rates of 3.27% in 2016 compared to 2.82% in 2015.
- Pre-tax income contribution by Mobile Modular, TRS-RenTelco and Adler Tanks was 44%, 35% and 16%, respectively, compared to 29%, 38% and 34%, respectively, for the comparable 2015 period. These results are discussed on a segment basis below. Enviroplex pre-tax income contribution was 5% in 2016 compared to a negative 1% in 2015.
- Adjusted EBITDA increased \$0.6 million, or 2%, to \$39.3 million in 2016.

Mobile Modular

For the three months ended June 30, 2016, Mobile Modular's total revenues increased \$7.6 million, or 18%, to \$49.7 million compared to the same period in 2015, primarily due to higher rental, rental related services and sales revenues. The revenue increase, together with higher gross margin on rental and rental related services, partly offset by higher selling and administrative expenses, resulted in a 64% increase in pre-tax income to \$6.6 million for the three months ended June 30, 2016, from \$4.0 million for the same period in 2015.

The following table summarizes quarterly results for each revenue and gross profit category, income from operations, pre-tax income and other selected information.

Mobile Modular – Three Months Ended 6/30/16 compared to Three Months Ended 6/30/15 (Unaudited)

(dollar amounts in thousands)	Three Months Ended		Increase (Decrease)	
	June 30, 2016	2015	\$	%
Revenues				
Rental	\$31,637	\$27,680	\$3,957	14%
Rental related services	12,132	10,488	1,644	16%
Rental operations	43,769	38,168	5,601	15%
Sales	5,785	3,831	1,954	51%
Other	125	121	4	3%
Total revenues	49,679	42,120	7,559	18%
Costs and Expenses				
Direct costs of rental operations:				
Depreciation of rental equipment	5,221	4,719	502	11%
Rental related services	8,331	7,388	943	13%
Other	11,229	10,740	489	5%
Total direct costs of rental operations	24,781	22,847	1,934	8%
Costs of sales	4,264	2,711	1,553	57%
Total costs of revenues	29,045	25,558	3,487	14%
Gross Profit				
Rental	15,188	12,221	2,967	24%
Rental related services	3,801	3,100		