

Blue Bird Corp
Form 10-Q
August 04, 2017
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 July 1, 2017

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 001-36267

BLUE BIRD CORPORATION

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

46-3891989

(I.R.S. Employer
Identification No.)

402 Blue Bird Boulevard, Fort Valley, Georgia 31030

(Address of principal executive offices)

(Zip Code)

(478) 822-2801

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes 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, 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

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Non-accelerated filer (Do not check if a smaller reporting company) 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

As of July 31, 2017, there were issued and outstanding 24,233,924 shares of the registrant's common stock, \$0.0001 par value.

BLUE BIRD CORPORATION
FORM 10-Q

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Cautionary Note Regarding Forward-Looking Statements

This Quarterly Report on Form 10-Q (this “Report”) of Blue Bird Corporation (“Blue Bird” or the “Company”) contains forward-looking statements. Except as otherwise indicated by the context, references in this Report to “we,” “us” and “our” are to the consolidated business of the Company. All statements in this Report, including those made by the management of the Company, other than statements of historical fact, are forward-looking statements. These forward-looking statements are based on management’s estimates, projections and assumptions as of the date hereof and include the assumptions that underlie such statements. Forward-looking statements may contain words such as “may,” “will,” “should,” “could,” “would,” “expect,” “plan,” “estimate,” “project,” “forecast,” “seek,” “target,” “anticipate,” “predict,” “potential” and “continue,” the negative of these terms, or other comparable terminology. Examples of forward-looking statements include statements regarding the Company’s future financial results, research and development results, regulatory approvals, operating results, business strategies, projected costs, products, competitive positions, management’s plans and objectives for future operations, and industry trends. These forward-looking statements relate to expectations for future financial performance, business strategies or expectations for our business. Specifically, forward-looking statements may include statements relating to:

- the future financial performance of the Company;
- changes in the market for Blue Bird products; and
- expansion plans and opportunities.

These forward-looking statements are based on information available as of the date of this Report (or, in the case of forward-looking statements incorporated herein by reference, as of the date of the applicable filed document), and current expectations, forecasts and assumptions, and involve a number of judgments, risks and uncertainties. Accordingly, forward-looking statements should not be relied upon as representing our views as of any subsequent date, and we do not undertake any obligation to update forward-looking statements to reflect events or circumstances after the date they were made, whether as a result of new information, future events or otherwise, except as may be required under applicable securities laws. As a result of a number of known and unknown risks and uncertainties, our actual results or performance may be materially different than those expressed or implied by these forward-looking statements.

Any expectations based on these forward-looking statements are subject to risks and uncertainties and other important factors, including those discussed in the reports we file with the Securities and Exchange Commission (the “SEC”), specifically the sections titled “Risk Factors” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in the Company’s 2016 Form 10-K, filed with the SEC on December 15, 2016. Other risks and uncertainties are and will be disclosed in the Company’s prior and future SEC filings. The following information should be read in conjunction with the financial statements included in the Company’s 2016 Form 10-K, filed with the SEC on December 15, 2016.

Available Information

We are subject to the reporting and information requirements of the Securities Exchange Act of 1934, as amended, and as a result are obligated to file annual, quarterly, and current reports, proxy statements, and other information with the SEC. We make these filings available free of charge on our website (<http://www.blue-bird.com>) as soon as reasonably practicable after we electronically file them with, or furnish them to, the SEC. Information on our website does not constitute part of this Quarterly Report on Form 10-Q. In addition, the SEC maintains a website (<http://www.sec.gov>) that contains our annual, quarterly, and current reports, proxy and information statements, and other information we electronically file with, or furnish to, the SEC. Any materials we file with, or furnish to, the SEC may also be read and/or copied at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Information on the operation of the Public Reference Room may be obtained by calling the SEC at 1-800-SEC-0330.

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited).

BLUE BIRD CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

(in thousands except for share data)	July 1, 2017	October 1, 2016
Assets		
Current assets		
Cash and cash equivalents	\$50,311	\$52,309
Accounts receivable, net	34,180	20,315
Inventories	126,602	53,806
Other current assets	12,074	6,104
Total current assets	\$223,167	\$132,534
Property, plant and equipment, net	34,156	33,466
Goodwill	18,825	18,825
Intangible assets, net	57,984	59,491
Equity investment in affiliate	13,455	12,944
Deferred tax assets	18,289	19,080
Other assets	904	1,526
Total assets	\$366,780	\$277,866
Liabilities and Stockholders' Deficit		
Current liabilities		
Accounts payable	\$135,417	\$80,646
Warranty	8,316	7,972
Accrued expenses	20,976	20,455
Deferred warranty income	6,508	5,666
Other current liabilities	11,138	4,032
Current portion of long-term debt	8,000	11,750
Total current liabilities	\$190,355	\$130,521
Long-term liabilities		
Long-term debt	\$145,028	\$140,366
Warranty	11,966	11,472
Deferred warranty income	12,022	10,521
Other liabilities	15,131	15,592
Pension	51,910	56,368
Total long-term liabilities	\$236,057	\$234,319
Guarantees, commitments and contingencies (Note 6)		
Stockholders' deficit		
Preferred stock, \$0.0001 par value, 10,000,000 shares authorized, 500,000 issued with liquidation preference of \$50,000	\$50,000	\$50,000
Common stock, \$0.0001 par value, 100,000,000 shares authorized, 23,730,211 and 22,518,058 issued and outstanding at July 1, 2017 and October 1, 2016, respectively	2	2
Additional paid-in capital	60,760	50,771
Accumulated deficit	(114,599)	(128,856)
Accumulated other comprehensive loss	(55,795)	(58,891)
Total stockholders' deficit	\$(59,632)	\$(86,974)
Total liabilities and stockholders' deficit	\$366,780	\$277,866

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

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BLUE BIRD CORPORATION AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)
 (Unaudited)

(in thousands except for share data)	Three Months Ended		Nine Months Ended	
	July 1, 2017	July 2, 2016	July 1, 2017	July 2, 2016
Net sales	\$332,604	\$323,055	\$677,915	\$645,596
Cost of goods sold	287,594	276,247	590,058	554,921
Gross profit	\$45,010	\$46,808	\$87,857	\$90,675
Operating expenses				
Selling, general and administrative expenses	16,331	45,505	53,782	81,329
Operating profit	\$28,679	\$1,303	\$34,075	\$9,346
Interest expense	(1,398)	(4,040)	(5,801)	(12,736)
Interest income	50	7	63	118
Other (expense) income, net	(11)	—	13	16
Loss on debt extinguishment	—	—	(10,142)	—
Income (loss) before income taxes	\$27,320	\$(2,730)	\$18,208	\$(3,256)
Income tax expense	(8,302)	(887)	(5,806)	(2,069)
Equity in net income of non-consolidated affiliate	1,036	696	1,997	1,494
Net income (loss) from continuing operations	\$20,054	\$(2,921)	\$14,399	\$(3,831)
Loss from discontinued operations, net of tax	(22)	(13)	(142)	(46)
Net income (loss)	\$20,032	\$(2,934)	\$14,257	\$(3,877)
Defined benefit pension plan, net of tax expense of \$566, \$419, \$1,698, and \$1,257, respectively	1,007	777	3,020	2,333
Cash flow hedge (loss) gain, net of tax (benefit) expense of (\$13), (\$33), \$41, and (\$149), respectively	(26)	(60)	76	(276)
Comprehensive income (loss)	\$21,013	\$(2,217)	\$17,353	\$(1,820)
Earnings per share:				
Net income (loss) (from above)	\$20,032	\$(2,934)	\$14,257	\$(3,877)
Less: preferred stock dividends	974	964	2,944	2,915
Net income (loss) available to common stockholders	\$19,058	\$(3,898)	\$11,313	\$(6,792)
Basic weighted average shares outstanding	23,659,057	21,084,878	23,101,685	20,989,737
Diluted weighted average shares outstanding	29,527,612	21,084,878	24,654,158	20,989,737
Basic earnings (loss) per share, continuing operations	\$0.81	\$(0.18)	\$0.50	\$(0.32)
Basic earnings (loss) per share, discontinued operations	—	—	(0.01)	—
Basic earnings (loss) per share	\$0.81	\$(0.18)	\$0.49	\$(0.32)
Diluted earnings (loss) per share, continuing operations	\$0.68	\$(0.18)	\$0.46	\$(0.32)
Diluted earnings (loss) per share, discontinued operations	—	—	—	—
Diluted earnings (loss) per share	\$0.68	\$(0.18)	\$0.46	\$(0.32)

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

BLUE BIRD CORPORATION AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (Unaudited)

(in thousands of dollars)	Nine Months Ended	
	July 1, 2017	July 2, 2016
Cash flows from operating activities		
Net income (loss)	\$14,257	\$(3,877)
Loss from discontinued operations, net of tax	142	46
Adjustments to reconcile net income (loss) to net cash provided by continuing operations		
Depreciation and amortization	6,106	6,025
Amortization of debt costs	912	2,232
Share-based compensation	904	12,717
Unfunded portion of Phantom Equity Plan	—	1,355
Equity in net income of affiliate	(1,997)	(1,494)
(Gain) loss on disposal of fixed assets	(43)	29
Deferred taxes	(874)	8,461
Provision for bad debt	—	(5)
Amortization of deferred actuarial pension losses	4,718	3,590
Loss on debt extinguishment	10,142	—
Changes in assets and liabilities:		
Accounts receivable	(13,701)	(6,003)
Inventories	(72,796)	(52,232)
Other assets	(5,941)	(6,055)
Accounts payable	56,671	50,332
Accrued expenses, pension and other liabilities	6,060	3,870
Dividend from equity investment in affiliate	1,412	2,316
Total adjustments	\$(8,427)	\$25,138
Net cash provided by continuing operations	\$5,972	\$21,307
Net cash used in discontinued operations	(221)	(46)
Total cash provided by operating activities	\$5,751	\$21,261
Cash flows from investing activities		
Cash paid for fixed assets	(7,193)	(6,511)
Proceeds from sale of fixed assets	47	—
Total cash used in investing activities	\$(7,146)	\$(6,511)
Cash flows from financing activities		
Repayments under the former senior term loan	\$(161,500)	\$(33,812)
Borrowings under the new term loan	156,887	—
Repayments under the new term loan	(4,000)	—
Cash paid for capital leases	(117)	(168)
Cash paid for debt issuance costs	(299)	(1,117)
Cash paid to extinguish debt	(507)	—
Contributions from former majority stockholder	—	15,616
Payment of dividends on preferred stock	(2,944)	(1,917)
Cash paid for employee taxes on stock option exercises and vested restricted shares	(981)	(3,511)
Proceeds from exercises of warrants	12,858	—
Total cash used in financing activities	\$(603)	\$(24,909)
Change in cash and cash equivalents	(1,998)	(10,159)
Cash and cash equivalents, beginning of period	52,309	52,861
Cash and cash equivalents, end of period	\$50,311	\$42,702

(in thousands of dollars)	Nine Months Ended July	July 1, 2, 2017 2016
Supplemental disclosures of cash flow information		
Cash paid during the period for:		
Interest paid, net of interest received	4,775,411	
Income tax paid, net of tax refunds	1,318,073	
Non-cash Investing and Financing activities		
Capital expenditures funded by capital lease borrowings	—	100
Change in accounts payable for capital additions to property, plant and equipment	1,900 220	
Common stock dividend on Series A preferred stock (market value of common shares)	—	998
Cashless exercise of stock options	4,124	—
Cash receivable for warrant exercises	164	—
The accompanying notes are an integral part of these condensed consolidated financial statements.		

BLUE BIRD CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Nature of Business and Basis of Presentation

Nature of Business

On February 24, 2015, Hennessy Capital Acquisition Corp. ("HCAC") consummated its business combination (the "Business Combination"), pursuant to which HCAC acquired all of the outstanding capital stock of School Bus Holdings, Inc. ("SBH") from The Traxis Group B.V. (the "Seller" or "Traxis"). SBH operates its business of designing and manufacturing school buses through subsidiaries and under the Blue Bird Corporation ("Blue Bird") name. In the Business Combination, the total purchase price was paid in a combination of cash (\$100 million) and in shares of HCAC's Common Stock (12,000,000 shares valued at a total of \$120 million). In connection with the closing of the Business Combination, we changed our name from Hennessy Capital Acquisition Corp. to Blue Bird Corporation. Upon consummation of the Business Combination, SBH became a wholly-owned subsidiary of Blue Bird Corporation and SBH's direct and indirect subsidiaries became indirect subsidiaries of our parent corporation.

Pursuant to, and subject to the terms of, a Purchase and Sale Agreement, dated as of May 26, 2016 (the "Purchase Agreement"), by and among Traxis, ASP BB Holdings LLC, a Delaware limited liability company ("ASP"), and the Company, Traxis agreed to sell and ASP agreed to purchase all of the 12,000,000 shares of common stock, par value \$0.0001 (the "Common Stock"), of the Company owned by Traxis (the "Transaction Shares"). Subject to the terms and conditions set forth in the Purchase Agreement, ASP acquired 7,000,000 Transaction Shares at an initial closing on June 3, 2016 for an amount in cash equal to \$10.10 per share and 5,000,000 Transaction Shares at a second closing on June 8, 2016 for an amount in cash equal to \$11.00 per share, for an aggregate purchase price of \$125.7 million. There were no proceeds to the Company from this transaction. The sale of Transaction Shares triggered a phantom equity compensation payment. This payment was primarily funded by Traxis and not by the Company.

Blue Bird Body Company, a wholly-owned subsidiary of Blue Bird, was incorporated in 1958 and has manufactured, assembled and sold school buses to a variety of municipal, federal and commercial customers since 1927. The majority of Blue Bird's sales are made to an independent distributor network, which in turn sells buses to ultimate end users. We are headquartered in Fort Valley, Georgia. References in these notes to financial statements to "Blue Bird", the "Company," "we," "our," or "us" refer to Blue Bird Corporation and its wholly-owned subsidiaries, unless the context specifically indicates otherwise.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant inter-company transactions and accounts have been eliminated in consolidation.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial reporting and Article 8 of Regulation S-X. The Company's fiscal year ends on the Saturday closest to September 30 with its quarters consisting of thirteen weeks in most years. In fiscal year 2017, there are a total of 52 weeks. For fiscal years 2017 and 2016, the third quarters both included 13 weeks and the nine months ended both included 39 weeks.

In the opinion of management, all adjustments considered necessary for a fair presentation of financial results have been made. Such adjustments consist of only those of a normal recurring nature. Operating results for any interim period are not necessarily indicative of the results that may be expected for the entire year. Accordingly, they do not

include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

The Condensed Consolidated Balance Sheet data as of October 1, 2016 was derived from the Company's audited financial statements but do not include all disclosures required by generally accepted accounting principles. For additional information, including the Company's significant accounting policies, refer to the consolidated financial statements and related footnotes for the fiscal year ended October 1, 2016 as set forth in the Company's 2016 Form 10-K filed on December 15, 2016.

The Business Combination was accounted for as a reverse acquisition, since immediately following completion of the transaction, the sole stockholder of SBH immediately prior to the Business Combination maintained effective control of Blue Bird Corporation, the post-combination company. For accounting purposes, SBH is deemed the accounting acquirer in the transaction and, consequently, the transaction is treated as a recapitalization of SBH (i.e., a capital transaction involving the issuance of stock and payment of cash by HCAC for the stock of SBH). Accordingly, the consolidated assets, liabilities and results of operations of SBH are the historical financial statements of Blue Bird Corporation, and HCAC assets, liabilities and results of operations are consolidated with SBH beginning on the acquisition date. No step-up in basis of intangible assets or goodwill was recorded in this transaction. We have effected this treatment through opening stockholders' deficit by adjusting the number of our common shares outstanding. Other than transaction costs paid and a contribution from our majority stockholder for payment of management incentive compensation related to the transaction, the transaction was primarily non-cash and involved exchanges of consideration and equity between our majority stockholder and HCAC and its related entities.

Use of Estimates and Assumptions

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") requires management to make estimates and assumptions. At the date of the financial statements, these estimates and assumptions affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities, and during the reporting period, these estimates and assumptions affect the reported amounts of revenues and expenses. For example, significant management judgments are required in determining excess, obsolete, or unsalable inventory, allowance for doubtful accounts, potential impairment of long-lived assets, goodwill and intangibles, the accounting for self-insurance reserves, warranty reserves, pension obligations, income taxes, environmental liabilities and contingencies. Future events and their effects cannot be predicted with certainty, and, accordingly, the Company's accounting estimates require the exercise of judgment. The accounting estimates used in the preparation of the Company's condensed consolidated financial statements may change as new events occur, as more experience is acquired, as additional information is obtained and as the Company's operating environment changes. The Company evaluates and updates its assumptions and estimates on an ongoing basis and may employ outside experts to assist in the Company's evaluations. Actual results could differ from the estimates that the Company has used.

2. Summary of Significant Accounting Policies and Recent Accounting Standards

The Company's significant accounting policies are described in the Company's 2016 Form 10-K, filed with the SEC on December 15, 2016. Our senior management has reviewed these significant accounting policies and related disclosures and determined that there were no significant changes in our critical accounting policies in the nine months ended July 1, 2017.

Recently Adopted Accounting Standards

ASU 2015-17 — In November 2015, the FASB issued ASU No. 2015-17, Balance Sheet Classification of Deferred Taxes, which simplifies the presentation of deferred taxes by requiring deferred tax assets and liabilities to be classified as non-current on the balance sheet. The standard is effective for public companies for annual reporting periods beginning after December 15, 2016, and interim periods within those fiscal years. The guidance may be adopted prospectively or retrospectively and early adoption is permitted. The Company elected to early adopt this standard on a retrospective basis in the first quarter of fiscal 2017, and reclassified \$7.6 million of current deferred tax assets to long-term deferred tax assets, resulting in a total of \$19.1 million of long-term deferred tax assets at October 1, 2016, compared to the prior presentation of \$11.5 million. All future deferred tax assets and liabilities will be recorded as long-term.

3. Supplemental Financial Information

Inventory

The Company values inventories at the lower of cost or market value. The Company uses a standard costing methodology, which approximates cost on a first-in, first-out basis. The Company reviews the standard costs of raw materials, work-in-process and finished goods inventory on a periodic basis to ensure that its inventories approximate current actual costs. Manufacturing cost includes raw materials, direct labor and manufacturing overhead. The following table presents the components of inventory at the dates indicated:

(in thousands of dollars)	July 1, 2017	October 1, 2016
Raw materials	\$71,718	\$40,940
Work in process	39,008	10,011
Finished goods	15,876	2,855
Total inventory	\$126,602	\$53,806

Product Warranties

The Company's products are generally warranted against defects in material and workmanship for a period of one to five years. A provision for estimated warranty costs is recorded at the time the unit is sold. The methodology to determine warranty reserve calculates average expected warranty claims using warranty claims by body type, by month, over the life of the bus, which is then multiplied by remaining months under warranty, by warranty type. Management believes the methodology provides an accurate reserve estimate. Actual claims incurred could differ from the original estimates, requiring future adjustments.

The following table reflects activity in accrued warranty cost (current and long-term portion combined) for the periods presented:

(in thousands of dollars)	Three Months		Nine Months	
	Ended July 1, 2017	July 2, 2016	Ended July 1, 2017	July 2, 2016
Balance at beginning of period	\$18,612	\$16,768	\$19,444	\$17,661
Add current period accruals	3,775	3,691	7,555	7,195
Current period reductions of accrual	(2,105)	(1,956)	(6,717)	(6,353)
Balance at end of period	\$20,282	\$18,503	\$20,282	\$18,503

The Company also sells extended warranties related to its products. Revenue related to these contracts is recognized on a straight-line basis over the contract period and costs thereunder are expensed as incurred. All warranty expenses are recorded in the cost of goods sold line in the Condensed Consolidated Statements of Operations and Comprehensive Income (Loss). The methodology to determine the short-term extended warranty income reserve is based on twelve months of the remaining warranty value for each effective extended warranty at the balance sheet date.

The following table reflects activity in deferred warranty income (current and long-term portions combined), for the sale of extended warranties of two to five years, for the periods presented:

(in thousands of dollars)	Three Months		Nine Months	
	Ended July 1, 2017	July 2, 2016	Ended July 1, 2017	July 2, 2016
Balance at beginning of period	\$16,654	\$14,060	\$16,187	\$14,145
Add current period deferred income	3,396	2,952	6,769	5,446
Current period recognition of income	(1,520)	(1,261)	(4,426)	(3,840)
Balance at end of period	\$18,530	\$15,751	\$18,530	\$15,751

Self-Insurance

The following table reflects our total accrued self-insurance liability, comprised of workers compensation and health insurance related claims, at the dates indicated:

(in thousands of dollars)	July 1, 2017	October 1, 2016
Current portion	\$3,167	\$3,679
Long-term portion	2,396	2,786
Total accrued self-insurance	\$5,563	\$6,465

The current and long-term portions of the accrued self-insurance liability are reflected in accrued expenses and other liabilities, respectively, on the Condensed Consolidated Balance Sheets.

Shipping and Handling Revenues

Shipping and handling revenues represent costs billed to customers and are included in net sales. Shipping and handling costs incurred are included in cost of goods sold. Shipping and handling revenues were \$6.6 million and \$6.2 million for the three months ended July 1, 2017 and July 2, 2016, respectively, and \$12.8 million and \$11.5 million for the nine months ended July 1, 2017 and July 2, 2016, respectively. The related cost of goods sold was \$6.0 million and \$5.7 million for the three months ended July 1, 2017 and July 2, 2016, respectively, and \$11.3 million and \$10.1 million for the nine months ended July 1, 2017 and July 2, 2016, respectively.

Pension Expense

Components of net periodic pension benefit cost were as follows for the periods presented:

(in thousands of dollars)	Three Months		Nine Months	
	Ended	Ended	Ended	Ended
	July 1, 2017	July 2, 2016	July 1, 2017	July 2, 2016
Interest cost	\$1,266	\$1,411	\$3,797	\$4,232
Expected return on plan assets	(1,590)	(1,528)	(4,769)	(4,584)
Amortization of prior loss	1,573	1,196	4,718	3,590
Net periodic benefit cost	\$1,249	\$1,079	\$3,746	\$3,238
Amortization of prior loss, recognized in other comprehensive income	1,573	1,196	4,718	3,590
Total recognized in net periodic pension benefit cost and other comprehensive income	\$(324)	\$(117)	\$(972)	\$(352)

Warrants

At July 1, 2017, there were a total of 7,180,466 warrants outstanding to purchase 3,590,233 shares of our Common Stock.

4. Debt

On December 12, 2016, Blue Bird Body Company, a wholly-owned subsidiary of the Company, executed a \$235.0 million five-year credit agreement provided by Bank of Montreal, which acts as the administrative agent and an issuing bank, Fifth Third Bank, as co-syndication agent and an issuing bank, and Regions Bank, as Co-Syndication Agent, together with other lenders (the "Credit Agreement").

The credit facility provided for under the Credit Agreement consists of a term loan facility in an aggregate initial principal amount of \$160.0 million (the "Term Loan Facility") and a revolving credit facility with aggregate commitments of \$75.0 million. The revolving credit facility includes a \$15.0 million letter of credit sub-facility and a \$5.0 million swingline sub-facility (the "Revolving Credit Facility," and together with the Term Loan Facility, each a "Credit Facility" and collectively, the "Credit Facilities"). As a result of the Credit Agreement, we incurred \$3.3 million of debt discount and issuance costs, which have been recorded as contra-debt and will be amortized over the life of the Credit Agreement using the effective interest method. Proceeds from the Term Loan Facility were used to fully extinguish our previous credit agreement with Societe Generale. In connection with the extinguishment, we recorded a \$10.1 million loss, which was the difference in the reacquisition price of the extinguished debt and the net carrying value at extinguishment. The loss includes the write-off of unamortized deferred financing costs recorded as a reduction of the prior debt, unamortized issuance costs associated with the previous revolving credit facility recorded in other assets, as well as interest and legal fees incurred to extinguish the prior debt.

The interest rate on the Term Loan Facility is (i) from the Closing Date until April 1, 2017, an election of either base rate plus 1 point or LIBOR plus 2 points and (ii) commencing with the fiscal quarter ending on April 1, 2017 and thereafter, dependent on the Total Net Leverage Ratio (as defined below) of the Company, an election of either base rate or LIBOR pursuant to the table below:

Level	Total Net Leverage Ratio	ABR Loans	Eurodollar Loans
I	Less than 2.00x	0.75%	1.75%
II	Greater than or equal to 2.00x and less than 2.50x	1.00%	2.00%
III	Greater than or equal to 2.50x and less than 3.00x	1.25%	2.25%
IV	Greater than or equal to 3.00x	1.50%	2.50%

Debt consisted of the following at the dates indicated:

(in thousands of dollars)	July 1, 2017	October 1, 2016
2021 term loan, net of deferred financing costs of \$2,972	\$153,028	\$—
2020 term loan, net of deferred financing costs of \$9,384	—	152,116
Less: Current portion of long-term debt	8,000	11,750
Long-term debt, net of current portion	\$145,028	\$140,366

Term loans are recognized on the Condensed Consolidated Balance Sheets at the unpaid principal balance, and are not subject to fair value measurement; however, given the variable rates on the loans, the Company estimates that the unpaid principal balance approximates fair value. If measured at fair value in the financial statements, the term loans would be classified as Level 2 in the fair value hierarchy. At July 1, 2017 and October 1, 2016, \$156.0 million and \$161.5 million, respectively, were outstanding on the term loans.

At July 1, 2017 and October 1, 2016, the stated interest rates on the term loans were 2.8% and 6.5%, respectively. At July 1, 2017 and October 1, 2016, the weighted-average annual effective interest rates for the term loans were 4.8% and 8.3%, respectively, which included amortization of the deferred financing costs.

No borrowings were outstanding on the Revolving Credit Facility at July 1, 2017, however, since there were \$5.1 million of Letters of Credit outstanding on July 1, 2017, the Company would have been able to borrow \$69.9 million on the revolving line of credit.

Interest expense on all indebtedness was \$1.4 million and \$4.0 million for the three months ended July 1, 2017 and July 2, 2016, respectively, and \$5.8 million and \$12.7 million for the nine months ended July 1, 2017 and July 2, 2016, respectively.

The schedules of remaining principal maturities for the term loan for the next five fiscal years are as follows:
(in thousands of dollars)

Year	Principal Payments
2017	\$2,000
2018	8,000
2019	8,000
2020	11,000
2021	15,000
Thereafter	112,000
Total remaining principal payments	\$156,000

5. Income Taxes

Income tax provisions for interim periods are based on estimated annual income tax rates, adjusted to reflect the effects of any significant infrequent or unusual items which are required to be discretely recognized within the current interim period. The effective tax rates in the periods presented are largely based upon the forecast pre-tax earnings mix and allocation of certain expenses in various taxing jurisdictions where the Company conducts its business, primarily the United States.

The effective tax rate for the three month period ended July 1, 2017 was 30.4%, which differed from the statutory federal income tax rate of 35% due mainly to tax rate benefit items such as the domestic production activities deduction, foreign tax credits, and stock option deductions in excess of recorded expense. These benefits were partially offset by discrete expense items, the largest being interest and penalties on uncertain tax positions. The

effective tax rate for the three month period ended July 2, 2016 was (32.5)% and differed from the statutory federal income tax rate of 35%, primarily from discrete items in the period, including interest and penalties on uncertain tax positions and a net tax shortfall from the vesting of share-based compensation awards pursuant to the adoption of ASU 2016-09, which were partially offset by the benefit from operating losses in the period.

The effective tax rate for the nine month period ended July 1, 2017 was 31.9% and differed from the statutory federal income tax rate of 35% primarily from tax rate benefit items such as the domestic production activities deduction, foreign tax credits, and stock option deductions in excess of recorded expense. These benefits were partially offset by discrete expense items, the largest being interest and penalties on uncertain tax positions. The effective tax rate for the nine month period ended July 2, 2016 was (63.5)% and differed from the statutory federal income tax rate of 35%, primarily from discrete items increasing tax expense in the year to date period, including a change in investor tax on our non-consolidated affiliate income, the application of tax credits claimed as offsets against our payroll tax liabilities, interest and penalties on uncertain tax positions, the vesting of share-based compensation awards pursuant to the adoption of

ASU 2016-09, which were partially offset by recording the impact of new tax legislation and by the benefit from operating losses in the period.

6. Guarantees, Commitments and Contingencies

Litigation

At July 1, 2017, the Company had a number of product liability and other cases pending. Management believes that, considering the Company's insurance coverage and its intention to vigorously defend its positions, the ultimate resolution of these matters will not have a material adverse effect on the Company's financial statements.

Environmental

The Company is subject to a variety of environmental regulations relating to the use, storage, discharge and disposal of hazardous materials used in its manufacturing processes. Failure by the Company to comply with present and future regulations could subject it to future liabilities. In addition, such regulations could require the Company to acquire costly equipment or to incur other significant expenses to comply with environmental regulations. The Company is currently not involved in any material environmental proceedings and therefore management believes that the resolution of environmental matters will not have a material adverse effect on the Company's financial statements.

7. Segment Information

We manage our business in two operating segments, which are also our reportable segments. The Bus segment includes the manufacturing and assembly of buses to be sold to a variety of customers across the United States, Canada and in international markets. The Parts segment consists primarily of the purchase of parts from third parties to be sold to dealers within the Company's network. Financial information is reported on the basis that it is used internally by the chief operating decision maker (the "CODM") in evaluating segment performance and deciding how to allocate resources. The President and Chief Executive Officer of the Company has been identified as the CODM. Management evaluates the segments based primarily upon revenues and gross profit. A measure of assets is not applicable, as segment assets are not regularly reviewed by the CODM for evaluating performance or allocating resources. The tables below present segment net sales and gross profit for the periods presented:

Net sales

(in thousands of dollars)	Three Months Ended		Nine Months Ended	
	July 1, 2017	July 2, 2016	July 1, 2017	July 2, 2016
	Bus	\$317,333	\$309,432	\$633,499
Parts	15,271	13,623	44,416	40,764
Segment net sales	\$332,604	\$323,055	\$677,915	\$645,596

Gross profit

(in thousands of dollars)	Three Months Ended		Nine Months Ended	
	July 1, 2017	July 2, 2016	July 1, 2017	July 2, 2016
	Bus	\$39,843	\$41,594	\$72,234
Parts	5,167	5,214	15,623	15,567
Segment gross profit	\$45,010	\$46,808	\$87,857	\$90,675

The following table is a reconciliation of segment gross profit to consolidated income (loss) before income taxes for the periods presented:

(in thousands of dollars)	Three Months		Nine Months	
	Ended		Ended	
	July 1, 2017	July 2, 2016	July 1, 2017	July 2, 2016
Segment gross profit	\$45,010	\$46,808	\$87,857	\$90,675
Adjustments:				
Selling, general and administrative expenses	(16,331)	(45,505)	(53,782)	(81,329)
Interest expense	(1,398)	(4,040)	(5,801)	(12,736)
Interest income	50	7	63	118
Other income, net	(11)	—	13	16
Loss on debt extinguishment	—	—	(10,142)	—
Income (loss) before income taxes	\$27,320	\$(2,730)	\$18,208	\$(3,256)

Sales are attributable to geographic areas based on customer location and were as follows for the periods presented:

(in thousands of dollars)	Three Months		Nine Months Ended	
	Ended		Ended	
	July 1, 2017	July 2, 2016	July 1, 2017	July 2, 2016
United States	\$291,672	\$298,532	\$608,350	\$591,549
Canada	40,550	21,642	66,535	46,261
Rest of world	382	2,881	3,030	7,786
Total net sales	\$332,604	\$323,055	\$677,915	\$645,596

8. Foreign Exchange Contracts

The Company enters into foreign exchange swaps as economic hedges of anticipated cash flows denominated in Canadian Dollars. The contracts are entered into to protect against the risk that the eventual cash flows resulting from certain transactions would be affected by changes in exchange rates between the U.S. Dollar and the Canadian Dollar. At July 1, 2017, the Company had seven foreign exchange swap contracts with an aggregate notional amount of \$15.6 million. The foreign exchange contracts qualify for hedge accounting and have been designated as cash flow hedges with the effective portion of the gain or loss on the derivative instruments recorded in other comprehensive income until the underlying transactions occur. Once the anticipated transactions occur, the gain or loss on the swaps is recorded in current period earnings on the Consolidated Statements of Operations and Comprehensive Income (Loss).

The fair value of the foreign exchange contracts is based on the forward contract rates, which classifies as a Level 2 fair value measurement. At July 1, 2017, the fair value of all foreign exchange contracts was \$0.1 million and included in "other current assets" on the Consolidated Balance Sheet. At October 1, 2016, the fair value of the foreign exchange contracts was \$(0.2) million and included in "other current liabilities" on the Consolidated Balance Sheet.

The table below presents the effect of the Company's cash flow hedges for the periods presented:

(in thousands of dollars)	Location	Three Months		Nine Months	
		Ended		Ended	
		July 1, 2017	July 2, 2016	July 1, 2017	July 2, 2016
Foreign Exchange Contracts					
Amount of (loss) gain recognized in income on derivatives (effective portion)	OCI	\$(39)	\$(93)	\$344	\$(425)

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Amount of loss (gain) reclassified from AOCI into income (effective portion)	Other expense	—	—	(227)	—
Total amount recognized in other comprehensive (loss) income		\$(39)	\$(93)	\$117	\$(425)

All amounts in accumulated other comprehensive income (loss) are expected to be reclassified into earnings during the next 12 months.

9. Earnings Per Share

The following table presents the earnings per share computation for the periods presented:

(in thousands except for share data)	Three Months Ended		Nine Months Ended	
	July 1, 2017	July 2, 2016	July 1, 2017	July 2, 2016
Numerator:				
Net income (loss)	\$20,032	\$ (2,934)	\$14,257	\$ (3,877)
Less: Loss from discontinued operations, net of tax	(22)	(13)	(142)	(46)
Income (loss) from continuing operations, net of tax	20,054	(2,921)	14,399	(3,831)
Less: convertible preferred stock dividends	974	964	2,944	2,915
Income (loss) from continuing operations available to common stockholders, net of tax	\$19,080	\$ (3,885)	\$11,455	\$ (6,746)
Basic earnings per share (1):				
Weighted average common shares outstanding	23,659,057	21,084,878	23,101,685	20,989,737
Basic earnings per share, continuing operations	0.81	(0.18)	0.50	(0.32)
Basic earnings per share, discontinued operations	—	—	(0.01)	—
Basic earnings per share	\$0.81	\$ (0.18)	\$0.49	\$ (0.32)
Diluted earnings per share (2):				
Weighted average common shares outstanding	23,659,057	21,084,878	23,101,685	20,989,737
Weighted average dilutive securities, convertible preferred stock	4,314,064	—	—	—
Weighted average dilutive securities, restricted stock	2,383	—	484	—
Weighted average dilutive securities, warrants	1,326,916	—	1,314,161	—
Weighted average dilutive securities, stock options	225,192	—	237,828	—
Weighted average shares and dilutive potential common shares	29,527,612	21,084,878	24,654,158	20,989,737
Diluted earnings per share, continuing operations	0.68	(0.18)	0.46	(0.32)
Diluted earnings per share, discontinued operations	—	—	—	—
Diluted earnings per share	\$0.68	\$ (0.18)	\$0.46	\$ (0.32)

(1) Basic earnings per share is calculated by dividing income available to common stockholders from continuing operations, discontinued operations, and net income by the weighted average common shares outstanding during the period.

(2) Diluted earnings per share is calculated by adjusting the weighted average shares outstanding for the dilutive effect of common stock equivalents outstanding during the period, determined by using the treasury-stock method, and adjusting for the dilutive effect of our convertible preferred stock, determined by using the if-converted method. For the nine months ended July 1, 2017, 4,314,064 shares of convertible preferred stock were excluded from the dilutive calculation as the if-converted impact would be anti-dilutive. We incurred a net loss for the three and nine months ended July 2, 2016. As a result, basic and diluted shares outstanding are equal to each other for those periods due to the exclusion of potentially dilutive shares from the calculation of earnings per share as the effect would be anti-dilutive. For the three and nine months ended July 2, 2016, potentially dilutive shares excluded from the calculation were 4,417,141 and 4,356,032, respectively.

10. Share-Based Compensation

Restricted Stock Awards

The following table summarizes the Company's restricted stock ("RSAs") and restricted stock units ("RSUs") award activity for the period presented:

Restricted Stock Activity	Nine Months Ended July 1, 2017	
	Number of Shares	Weighted-Average Grant Date Fair Value
Balance, beginning of period	—	\$ —
Granted	77,451	15.82
Balance, end of period	77,451	15.82

Compensation expense for restricted stock awards, recognized in selling, general and administrative expenses on the Condensed Consolidated Statements of Operations and Comprehensive Income (Loss), was \$0.4 million and \$0.6 million with associated tax benefits of \$0.1 million and \$0.2 million for the three and nine months ended July 1, 2017, respectively. At July 1, 2017, unrecognized compensation cost related to restricted stock awards totaled \$0.7 million and is expected to be recognized over a weighted-average period of seven months.

Stock Option Awards

The following table summarizes the Company's stock option activity for the period presented:

Stock Option Award Activity	Nine Months Ended July 1, 2017	
	Number of Options	Weighted Average Exercise Price per Share (\$)
Outstanding options, beginning of period	918,749	\$ 10.08
Granted	133,484	15.50
Exercised (1)	(409,044)	10.08
Outstanding options, end of period (2)	643,189	11.20
Fully vested and exercisable options, end of period (3)	509,705	10.07

(1) Stock options exercised in the period had an aggregate intrinsic value totaling \$2.2 million.

(2) Stock options outstanding at the end of the period had an aggregate intrinsic value totaling \$3.7 million.

(3) Fully vested and exercisable options at the end of the period had an aggregate intrinsic value totaling \$3.5 million with a weighted average contractual remaining term of 7.8 years.

Compensation expense for stock option awards, recognized in selling, general and administrative expenses on the Consolidated Statements of Operations and Comprehensive Income (Loss), was \$0.1 million and \$0.3 million with associated tax benefits of \$0.0 million and \$0.1 million for the three and nine months ended July 1, 2017, respectively. At July 1, 2017, unrecognized compensation cost related to stock option awards totaled \$0.4 million and is expected to be recognized over a weighted-average period of six months.

The fair value of each option award at grant date was estimated using the Black-Scholes option-pricing model with the following assumptions and resulting grant-date fair value during the period presented:

	Nine Months Ended July 1, 2017
Expected volatility	33.7 %
Expected dividend yield	0 %
Risk-free interest rate	1.94 %
Expected term (in years)	5.5
Weighted-average grant-date fair value	\$5.35

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

The following discussion and analysis of financial condition and results of operations of the Company should be read in conjunction with the Company's unaudited financial statements for the three and nine months ended July 1, 2017 and July 2, 2016 and related notes appearing elsewhere in this Report. Our actual results may not be indicative of future performance. This discussion and analysis contains forward-looking statements and involves numerous risks and uncertainties, including, but not limited to, those discussed or incorporated by reference in the sections of this Report titled "Cautionary Note Regarding Forward-Looking Statements" and "Risk Factors". Actual results may differ materially from those contained in any forward-looking statements. Certain monetary amounts, percentages and other figures included in this Report have been subject to rounding adjustments. Accordingly, figures shown as totals in certain tables may not be the arithmetic aggregation of the figures that precede them, and figures expressed as percentages in the text may not total 100% or, as applicable, when aggregated, may not be the arithmetic aggregation of the percentages that precede them.

We refer to the fiscal year ended October 1, 2016 as "fiscal 2016". We refer to the quarter ended July 1, 2017 as the "third quarter of fiscal 2017" and we refer to the quarter ended July 2, 2016 as the "third quarter of fiscal 2016". There were 13 weeks in the third quarters of both fiscal 2017 and fiscal 2016.

Introductory Note

On February 24, 2015, the Company consummated a business combination (the "Business Combination"), pursuant to which the Company acquired all of the outstanding capital stock of School Bus Holdings Inc. ("School Bus Holdings" or "SBH") from The Traxis Group, B.V. (the "Seller"), in accordance with the purchase agreement, dated as of September 21, 2014, by and among the Company, the Seller and, solely for purposes of Section 10.01(a) thereof, Hennessy Capital Partners I LLC (the "HCAC Sponsor"), as amended on February 10, 2015 and February 18, 2015 (as so amended, the "Purchase Agreement"). Pursuant to the Purchase Agreement, the total purchase price was paid in a combination of cash in the amount of \$100.0 million and 12,000,000 shares of the Company's Common Stock valued at \$120.0 million.

In connection with the closing of the Business Combination, the Company changed its name from Hennessy Capital Acquisition Corp. to Blue Bird Corporation. Unless expressly stated otherwise in this Report, Blue Bird Corporation shall be referred to as "Blue Bird" or the "Company," and includes its consolidated subsidiaries.

Pursuant to, and subject to the terms of, a Purchase and Sale Agreement, dated as of May 26, 2016 (the "Purchase and Sale Agreement"), by and among Seller, ASP BB Holdings LLC, a Delaware limited liability company ("ASP"), and the Company, Seller agreed to sell and ASP agreed to purchase all of the 12,000,000 shares of Common Stock of the Company owned by Seller (the "Transaction Shares"). Subject to the terms and conditions set forth in the Purchase and Sale Agreement, ASP acquired 7,000,000 Transaction Shares at an initial closing on June 3, 2016 for an amount in cash equal to \$10.10 per share and 5,000,000 Transaction Shares at a second closing on June 8, 2016 for an amount in cash equal to \$11.00 per share, for an aggregate purchase price of \$125.7 million. There were no proceeds to the Company from this transaction. The sale of Transaction Shares triggered a phantom equity compensation payment which was primarily funded by Seller and not by the Company.

Executive Overview

Blue Bird is the leading independent designer and manufacturer of school buses. Our longevity and reputation in the school bus industry have made Blue Bird an iconic American brand. We distinguish ourselves from our principal competitors by dedicating our focus to the design, engineering, manufacture and sale of school buses and related parts. As the only principal manufacturer of chassis and body production specifically designed for school bus applications, Blue Bird is recognized as an industry leader for school bus innovation, safety, product quality/reliability/durability,

efficiency, and lower operating costs. In addition, Blue Bird is the market leader in alternative diesel fuel applications with its propane-powered, gasoline-powered, and compressed natural gas (“CNG”)-powered school buses.

Blue Bird sells its buses and aftermarket parts through an extensive network of United States and Canadian dealers that, in their territories, are exclusive to Blue Bird on Type C and D school buses. Blue Bird also sells directly to major fleet operators, the United States government, state governments and authorized dealers in a number of foreign countries.

Critical Accounting Policies and Estimates, Recent Accounting Pronouncements

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Blue Bird evaluates its estimates on an ongoing basis, based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Application of these accounting policies involves the exercise of judgment and use of assumptions as to future uncertainties and, as a result, actual results could differ from these estimates.

The Company's accounting policies that we believe are the most critical to aid in fully understanding and evaluating our reported financial results are described in the Company's 2016 Form 10-K, filed with the SEC on December 15, 2016 under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies and Estimates," which description is incorporated herein by reference. Our senior management has reviewed these critical accounting policies and related disclosures and determined that there were no significant changes in our critical accounting policies during the nine months ended July 1, 2017.

Recent Accounting Pronouncements

See discussion in Note 2 of Notes to Condensed Consolidated Financial Statements (Unaudited) included in Part I, Item 1 of this Report for a discussion of new and recently adopted accounting pronouncements.

Factors Affecting Our Revenues

Our revenues are driven primarily by the following factors:

Property tax revenues. Property tax revenues are one of the major sources of funding for new school buses. Property tax revenues are a function of land and building prices, relying on assessments of property value by state or county assessors and millage rates voted by the local electorate.

Student enrollment. Increases or decreases in the number of school bus riders have a direct impact on school district demand.

Revenue mix. We are able to charge more for certain of our products (e.g., Type C propane-powered school buses, Type D buses and buses with higher option content) than other products. The mix of products sold in any fiscal period can directly impact our revenues for the period.

Strength of the dealer network. We rely on our dealers, as well as a small number of major fleet operators, to be the direct point of contact with school districts and their purchasing agents. An effective dealer is capable of expanding revenues within a given school district by matching that district's needs to our capabilities, offering options that would not otherwise be provided to the district.

Pricing. Our products are sold to school districts throughout the United States and Canada. Each state and each Canadian province has its own set of regulations that govern the purchase of products, including school buses, by their school districts. We and our dealers must navigate these regulations, purchasing procedures and the districts' specifications in order to reach mutually acceptable price terms. Pricing may or may not be favorable to us, depending upon a number of factors impacting purchasing decisions.

Buying patterns of major fleets. Major fleets regularly compete against one another for existing accounts. Fleets are also continuously trying to win the business of school districts that operate their own transportation services. These activities can have either a positive or negative impact on our sales, depending on the brand preference of the fleet that wins the business. Major fleets also periodically review their fleet sizes and replacement patterns due to funding availability as well as the profitability of existing routes. These actions can impact total purchases by fleets in a given year.

Seasonality. Our sales are subject to seasonal variation based on the school calendar. The peak season has historically been during our third and fourth fiscal quarters. Sales during the third and fourth fiscal quarters are typically greater

than the first and second fiscal quarters due to the desire of municipalities to have any new buses that they order available to them at the beginning of the new school year. There are, however, variations in the seasonal demands from year to year depending in large part upon municipal budgets, distinct replacement cycles and student enrollment. This seasonality and annual variations of this seasonality could impact the ability to compare results between fiscal periods.

Factors Affecting Our Expenses and Other Items

Our expenses and other line items in our unaudited Condensed Consolidated Statements of Operations and Comprehensive Income (Loss) are principally driven by the following factors:

Cost of goods sold. The components of our cost of goods sold consist of material costs (principally powertrain components, steel and rubber, as well as aluminum and copper), labor expense and overhead. Our cost of goods sold may vary from period to period in part due to changes in sales volume and in part due to efforts by certain suppliers to pass through the economics associated with key commodities, design changes with respect to specific components, design changes with respect to specific bus models, wage increases for plant labor, the productivity of plant labor, delays in receiving materials and other logistical problems and the impact of overhead items such as utilities.

Selling, general and administrative expenses. Our selling, general and administrative expenses include costs associated with our selling and marketing efforts, engineering, centralized finance, human resources, purchasing and information technology services, as well as other administrative matters and functions. In most instances, other than direct costs associated with sales and marketing programs, the principal component of these costs is salary expense. Changes from period to period are typically driven by the number of our employees, as well as by merit increases provided to experienced personnel.

Regulatory expenses. We must comply with laws, regulations and requirements for public companies, including certain provisions of the Sarbanes-Oxley Act and related SEC regulations, as well as NASDAQ listing requirements. Compliance with the requirements of being a public company increases operating expenses in order to pay employees, legal counsel and accountants to assist us in, among other things, external reporting, instituting and monitoring a more comprehensive compliance and board governance function, establishing and maintaining internal control over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act, and preparing and distributing periodic public reports in compliance with our obligations under the federal securities laws.

Interest expense. Our interest expense relates to costs associated with our debt instruments and reflects both the amount of indebtedness and the interest rate that we are required to pay on our debt. In December 2016, we entered into a new \$160.0 million first lien credit agreement and a new \$75.0 million revolving credit agreement. Proceeds from the agreement were used to fully extinguish our prior debt obligations.

Income taxes. We make estimates of the amounts to recognize for income taxes in each tax jurisdiction in which we operate. In addition, provisions are established for withholding taxes related to the transfer of cash between jurisdictions and for uncertain tax positions taken.

Equity in net income of non-consolidated affiliate. We include in this line item our share of income or loss from our investment in Micro Bird, our unconsolidated 50/50 Canadian joint venture.

Key Non-GAAP Financial Measures We Use to Evaluate Our Performance

This filing includes the following non-GAAP financial measures “Adjusted EBITDA”, “Adjusted EBITDA Margin”, and “Free Cash Flow” because management views these metrics as a useful way to look at the performance of our operations between periods and to exclude decisions on capital investment and financing that might otherwise impact the review of profitability of the business based on present market conditions.

Adjusted EBITDA is defined as income from continuing operations prior to interest income, interest expense, income taxes, and depreciation, amortization, and disposals, as adjusted to add back certain charges that we may record each year, such as stock-compensation expense and transaction costs, as these expenses are not considered an indicator of ongoing company performance. We define Adjusted EBITDA margin as Adjusted EBITDA as a percentage of net sales. Adjusted EBITDA and Adjusted EBITDA margin are not measures of performance defined in accordance with GAAP. The measures are used as a supplement to GAAP results in evaluating certain aspects of our business, as

described below.

We believe that Adjusted EBITDA and Adjusted EBITDA margin are useful to investors in evaluating our performance because the measures consider the performance of our operations, excluding decisions made with respect to capital investment, financing, and other expenses. We believe that the non-GAAP metrics offer additional financial metrics that, when coupled with the GAAP results and the reconciliation to GAAP results, provide a more complete understanding of our results of operations and the factors and trends affecting our business.

Adjusted EBITDA and Adjusted EBITDA margin should not be considered as alternatives to net income as an indicator of our performance or as alternatives to any other measure prescribed by GAAP as there are limitations to using such non-GAAP measures. Although we

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believe the non-GAAP measures may enhance the evaluation of our operating performance based on recent revenue generation and product/overhead cost control because they exclude the impact of prior decisions made about capital investment, financing, and other expenses, (i) other companies in Blue Bird's industry may define Adjusted EBITDA and Adjusted EBITDA margin differently than we do and, as a result, they may not be comparable to similarly titled measures used by other companies in Blue Bird's industry, and (ii) Adjusted EBITDA and Adjusted EBITDA margin exclude certain financial information that some may consider important in evaluating our performance.

We compensate for these limitations by providing disclosure of the differences between Adjusted EBITDA and Adjusted EBITDA margin and GAAP results, including providing a reconciliation to GAAP results, to enable investors to perform their own analysis of our operating results.

Our measure of "Free Cash Flow" is used in addition to and in conjunction with results presented in accordance with GAAP and free cash flow should not be relied upon to the exclusion of GAAP financial measures. Free cash flow reflects an additional way of viewing our liquidity that, when viewed with our GAAP results, provides a more complete understanding of factors and trends affecting our cash flows. We strongly encourage investors to review our financial statements and publicly-filed reports in their entirety and not to rely on any single financial measure.

We define free cash flow as net cash provided by/used in continuing operations minus cash paid for fixed assets. We use free cash flow, and ratios based on the free cash flow, to conduct and evaluate our business because, although it is similar to cash flow from operations, we believe it is a more conservative measure of cash flow since purchases of fixed assets and intangible assets are a necessary component of ongoing operations. In limited circumstances in which proceeds from sales of fixed or intangible assets exceed purchases, free cash flow would exceed cash flow from operations. However, since we do not anticipate being a net seller of fixed or intangible assets, we expect free cash flow to be less than operating cash flows.

Our Segments

We manage our business in two operating segments, which are also our reportable segments: (i) the Bus segment, which involves the design, engineering, manufacture and sales of school buses and extended warranties; and (ii) the Parts segment, which includes the sales of replacement bus parts. Financial information is reported on the basis that it is used internally by the chief operating decision maker ("CODM") in evaluating segment performance and deciding how to allocate resources to segments. The President and Chief Executive Officer of the Company has been identified as the CODM. Management evaluates the segments based primarily upon revenues and gross profit.

Consolidated Results of Operations for the Three Months Ended July 1, 2017 and July 2, 2016:

(in thousands of dollars)	Three Months Ended	
	July 1, 2017	July 2, 2016
Net sales	\$332,604	\$323,055
Cost of goods sold	287,594	276,247
Gross profit	\$45,010	\$46,808
Operating expenses		
Selling, general and administrative expenses	16,331	45,505
Operating profit	\$28,679	\$1,303
Interest expense	(1,398)	(4,040)
Interest income	50	7
Other expense, net	(11)	—
Income (loss) before income taxes	\$27,320	\$(2,730)
Income tax expense	(8,302)	(887)
Equity in net income of non-consolidated affiliate	1,036	696
Net income (loss) from continuing operations	\$20,054	\$(2,921)
Loss from discontinued operations, net of tax	(22)	(13)
Net income (loss)	\$20,032	\$(2,934)
Other financial data:		
Adjusted EBITDA	\$32,206	\$32,484
Adjusted EBITDA margin	9.7	% 10.1 %

The following provides the results of operations of Blue Bird's two reportable segments:

(in thousands of dollars)	Three Months Ended	
	July 1, 2017	July 2, 2016
Net Sales by Segment		
Bus	\$317,333	\$309,432
Parts	15,271	13,623
Total	\$332,604	\$323,055

Gross Profit by Segment

Bus	\$39,843	\$41,594
Parts	5,167	5,214
Total	\$45,010	\$46,808

Net sales. Total net sales were \$332.6 million for the third quarter of fiscal 2017, an increase of \$9.5 million, or 3.0%, compared to \$323.1 million for the third quarter of fiscal 2016, reflecting an increase in units booked, which were 3,849 units for the third quarter of fiscal 2017 compared to 3,768 units for the third quarter of fiscal 2016.

For the bus segment, the average net sales price per unit for the third quarter of fiscal 2017 was 0.4% higher than the price per unit for the third quarter of fiscal 2016. This increase in unit price mainly reflects product and customer mix changes.

Parts sales increased \$1.6 million, or 12.1%, for the third quarter of fiscal 2017 compared to the third quarter of fiscal 2016, primarily due to the expansion of product offerings as well as new incentive and shipping programs launched in 2017.

Cost of goods sold. Total cost of goods sold was \$287.6 million for the third quarter of fiscal 2017, an increase of \$11.3 million, or 4.1%, compared to \$276.2 million for the third quarter of fiscal 2016, reflecting increased bus segment cost of goods sold totaling \$9.7 million, or 3.6%, and increased parts segment cost of goods sold totaling \$1.7 million, or 20.2%. As a percentage of net sales, total cost of goods sold increased from 85.5% to 86.5%.

For the bus segment, the average cost of goods sold per unit for the third quarter of fiscal 2017 was higher compared to the average cost of goods sold per unit for the third quarter of fiscal 2016.

The \$1.7 million increase in parts segment cost of goods sold for the third quarter of fiscal 2017 compared to the third quarter of fiscal 2016 was primarily attributed to increased parts sales volume.

Operating profit. Operating profit was \$28.7 million for the third quarter of fiscal 2017, an increase of \$27.4 million, compared to an operating profit of \$1.3 million for the third quarter of fiscal 2016. Profitability was positively impacted by a decrease of \$29.2 million in selling, general and administrative expenses, which was partially offset by a decrease of \$1.8 million in gross profit. Selling, general and administrative expenses for the third quarter of fiscal 2016 included expenses incurred from the change in control of our former majority stockholder, of which \$17.1 million was a non-recurring special compensation expense and \$9.8 million more share-based compensation expense primarily due to an accelerated vesting of awards as a result of the change in control.

Interest expense. Interest expense was \$1.4 million for the third quarter of fiscal 2017, a decrease of \$2.6 million, or 65.4%, compared to \$4.0 million for the third quarter of fiscal 2016. The decrease was primarily attributed to lower average borrowing levels as well as a decrease in the interest rate resulting from the new credit facility we entered into in December 2016.

Income taxes. Income tax expense was \$8.3 million for the third quarter of fiscal 2017, compared to income tax expense of \$0.9 million for the third quarter of fiscal 2016.

The effective tax rate for the three month period ended July 1, 2017 was 30.4%, which differed from the statutory federal income tax rate of 35% due mainly to tax rate benefit items such as the domestic production activities deduction, foreign tax credits, and stock option deductions in excess of recorded expense. These benefits were partially offset by discrete expense items, the largest being interest and penalties on uncertain tax positions. The effective tax rate for the three month period ended July 2, 2016 was (32.5)% and differed from the statutory federal income tax rate of 35%, primarily from discrete items in the period, including interest and penalties on uncertain tax positions and a net tax shortfall from the vesting of share-based compensation awards pursuant to the adoption of ASU 2016-09, which were partially offset by the benefit from operating losses in the period.

Adjusted EBITDA. Adjusted EBITDA was \$32.2 million, or 9.7% of net sales, for the third quarter of fiscal 2017, a decrease of \$0.3 million, or 0.9%, compared to \$32.5 million, or 10.1% of net sales, for the third quarter of fiscal 2016. The decrease in adjusted EBITDA was primarily the result of decreased gross profit.

The following table sets forth a reconciliation of net income to adjusted EBITDA for the periods presented:

(in thousands of dollars)	Three Months Ended	
	July 1, 2017	July 2, 2016
Net income (loss)	\$20,032	\$(2,934)
Loss from discontinued operations, net of tax	(22)	(13)
Net income (loss) from continuing operations	\$20,054	\$(2,921)
Interest expense	1,398	4,040
Interest income	(50)	(7)
Income tax expense	8,302	887
Depreciation, amortization, and disposals	2,008	2,022
Special compensation payment	—	17,112
Business combination expenses	—	185
One-time post-retirement benefit adjustment	—	896
Share-based compensation	494	10,270
Adjusted EBITDA	\$32,206	\$32,484
Adjusted EBITDA margin (percentage of net sales)	9.7	% 10.1

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Consolidated Results of Operations for the Nine Months Ended July 1, 2017 and July 2, 2016:

(in thousands of dollars)	Nine Months Ended	
	July 1, 2017	July 2, 2016
Net sales	\$677,915	\$645,596
Cost of goods sold	590,058	554,921
Gross profit	\$87,857	\$90,675
Operating expenses		
Selling, general and administrative expenses	53,782	81,329
Operating profit	\$34,075	\$9,346
Interest expense	(5,801)	(12,736)
Interest income	63	118
Other income, net	13	16
Loss on debt extinguishment	(10,142	