

WESCO INTERNATIONAL INC

Form 10-K

February 22, 2017

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2016

or

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

For the transition period from _____ to _____

Commission file number 001-14989

WESCO International, Inc.

(Exact name of registrant as specified in its charter)

Delaware 25-1723342

(State or other jurisdiction of (I.R.S. Employer

incorporation or organization) Identification No.)

225 West Station Square Drive

Suite 700 15219

Pittsburgh, Pennsylvania (Zip Code)

(Address of principal executive offices)

(412) 454-2200

(Registrant's telephone number, including area code)

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of Class Name of Exchange on which registered

Common Stock, par value \$.01 per share New York Stock Exchange

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes No

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 at least the past 90 days. Yes No

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 at least the past 90 days. Yes No

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 at least the past 90 days. Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such file). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Edgar Filing: WESCO INTERNATIONAL INC - Form 10-K

(Do not check if a smaller reporting
company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No
The registrant estimates that the aggregate market value of the voting shares held by non-affiliates of the registrant was approximately \$2,166.6 million as of June 30, 2016, the last business day of the registrant's most recently completed second fiscal quarter, based on the closing price on the New York Stock Exchange for such stock. As of February 21, 2017, 48,720,648 shares of Common Stock, par value \$.01 per share, of the registrant were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE:

Part III of this Form 10-K incorporates by reference portions of the registrant's Proxy Statement for its 2017 Annual Meeting of Stockholders.

Table of Contents

TABLE OF CONTENTS

	Page
<u>PART I</u>	
<u>Item 1. Business</u>	<u>1</u>
<u>Item 1A. Risk Factors</u>	<u>9</u>
<u>Item 1B. Unresolved Staff Comments</u>	<u>13</u>
<u>Item 2. Properties</u>	<u>13</u>
<u>Item 3. Legal Proceedings</u>	<u>14</u>
<u>Item 4. Mine Safety Disclosures</u>	<u>14</u>
<u>PART II</u>	
<u>Item 5. Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	<u>15</u>
<u>Item 6. Selected Financial Data</u>	<u>17</u>
<u>Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>18</u>
<u>Item 7A. Quantitative and Qualitative Disclosures About Market Risks</u>	<u>32</u>
<u>Item 8. Financial Statements and Supplementary Data</u>	<u>33</u>
<u>Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	<u>73</u>
<u>Item 9A. Controls and Procedures</u>	<u>73</u>
<u>Item 9B. Other Information</u>	<u>73</u>
<u>PART III</u>	
<u>Item 10. Directors, Executive Officers and Corporate Governance</u>	<u>74</u>
<u>Item 11. Executive Compensation</u>	<u>74</u>
<u>Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	<u>74</u>
<u>Item 13. Certain Relationships and Related Transactions, and Director Independence</u>	<u>74</u>
<u>Item 14. Principal Accountant Fees and Services</u>	<u>74</u>
<u>PART IV</u>	
<u>Item 15. Exhibits and Financial Statement Schedules</u>	<u>75</u>
<u>Item 16. Form 10-K Summary</u>	<u>79</u>
<u>Signatures</u>	<u>81</u>
EX-10.28	
EX-21.1	
EX-23.1	
EX-31.1	
EX-31.2	
EX-32.1	
EX-32.2	
EX-101 INSTANCE DOCUMENT	
EX-101 SCHEMA DOCUMENT	
EX-101 CALCULATION LINKBASE DOCUMENT	
EX-101 LABELS LINKBASE DOCUMENT	
EX-101 PRESENTATION LINKBASE DOCUMENT	
EX-101 DEFINITION LINKBASE DOCUMENT	

Table of Contents

PART I

Item 1. Business.

In this Annual Report on Form 10-K, “WESCO” refers to WESCO International, Inc., and its subsidiaries and its predecessors unless the context otherwise requires. References to “we,” “us,” “our” and the “Company” refer to WESCO and its subsidiaries.

The Company

WESCO International, Inc. (“WESCO International”), incorporated in 1993 and effectively formed in February 1994 upon acquiring a distribution business from Westinghouse Electric Corporation, is a leading North American-based distributor of products and provider of advanced supply chain management and logistics services used primarily in industrial, construction, utility, and commercial, institutional and government (“CIG”) markets. We are a leading provider of electrical, industrial, and communications maintenance, repair and operating (“MRO”) and original equipment manufacturers (“OEM”) products, construction materials, and advanced supply chain management and logistics services. Our primary product categories include general supplies, wire, cable and conduit, communications and security, electrical distribution and controls, lighting and sustainability, and automation, controls and motors. We serve approximately 75,000 active customers globally through approximately 500 full service branches primarily located in North America, with operations in 14 additional countries and nine distribution centers located in the United States and Canada. The Company employs approximately 9,000 employees worldwide. We distribute over 1,000,000 products, grouped into six categories, from more than 25,000 suppliers, utilizing a highly automated, proprietary electronic procurement and inventory replenishment system.

In addition, we offer a comprehensive portfolio of value-added capabilities, which includes supply chain management, logistics and transportation, procurement, warehousing and inventory management, as well as kitting, limited assembly of products and system installation. Our value-added capabilities, extensive geographic reach, experienced workforce and broad product and supply chain solutions have enabled us to grow our business and establish a leading position in North America.

Industry Overview

We operate in highly fragmented markets that include thousands of small regional and locally based, privately owned competitors. According to one industry publication, in 2015, the latest year for which market data is available, the five largest full-line electrical distributors in North America, including WESCO, accounted for approximately 33% of an estimated \$100 billion-plus of electrical sales in North America. Our global account, integrated supply and OEM programs provide customers with regional, national, North American and global supply chain consolidation opportunities. The demand for these programs is driven primarily by the desire of companies to reduce operating expenses by outsourcing operational and administrative functions associated with the procurement, management and utilization of MRO supplies and OEM components. We believe that opportunities exist for expansion of these programs. The total potential in the United States for purchases of MRO and OEM supplies and services across all industrial distribution market segments and channels is estimated to be nearly \$500 billion per a combination of industry sources.

According to various industry sources, electrical distribution industry sales have grown low-single-digits on average over the past three years, despite a low-single-digit decline in 2016. Growth in recent years has been driven by new products, technologies and applications. It is estimated that approximately 75% of electrical products sold in the United States are delivered to the end user through the distribution channel.

Table of Contents

Markets and Customers

We have a large base of approximately 75,000 active customers across a diverse set of end markets. Our top ten customers accounted for approximately 13% of our sales in 2016. No one customer accounted for more than 4% of our sales in 2016.

The following table outlines our sales breakdown by end market:

Year Ended December 31, (percentages based on total sales)	2016	2015	2014
Industrial	36%	39%	42%
Construction	34%	32%	31%
Utility	16%	15%	14%
Commercial, Institutional and Government	14%	14%	13%

Industrial. Sales to industrial customers of MRO, OEM, and construction products and services accounted for approximately 36% of our sales in 2016, compared to 39% in 2015. Industrial sales product categories include a broad range of electrical equipment and supplies as well as lubricants, pipe, valves, fittings, fasteners, cutting tools, power transmission, and safety products. In addition, OEM customers require a reliable supply of assemblies and components to incorporate into their own products as well as value-added services such as supplier consolidation, design and technical support, just-in-time supply and electronic commerce, and supply chain management.

Construction. Sales of electrical and communications products to contractors accounted for approximately 34% of our sales in 2016, compared to 32% in 2015. Customers include a wide array of contractors and engineering, procurement and construction firms for industrial, infrastructure, commercial and data and broadband communications projects. Specific applications include projects for refineries, railways, hospitals, wastewater treatment facilities, data centers, security installations, offices, and modular and mobile homes. In addition to a wide array of electrical products, we offer contractors communications products for projects related to IT/network modernization, physical security upgrades, broadband deployments, network security, and disaster recovery.

Utility. Sales to utilities and utility contractors accounted for approximately 16% of our sales in 2016, compared to 15% in 2015. Customers include large investor-owned utilities, rural electric cooperatives, municipal power authorities and contractors that serve these customers. We provide our utility customers with products and services to support the construction and maintenance of their generation, transmission and distribution systems along with an extensive range of products that meet their power plant MRO and capital projects needs. Materials management and procurement outsourcing arrangements are also important in this market, as cost pressures and deregulation have caused utility customers to seek improvements in the efficiency and effectiveness of their supply chains.

Commercial, Institutional and Government ("CIG"). Sales to CIG customers accounted for approximately 14% of our sales in 2016 and 2015. Customers include schools, hospitals, property management firms, retailers and federal, state and local government agencies of all types, including federal contractors.

Business Strategy

Our goal is to grow organically at a rate greater than that of our industry while making accretive acquisitions. Our organic growth strategy focuses on enhancing our sales, technical expertise and customer service capabilities to acquire new customers and increase our sales to current customers, broaden our product and service offerings and expand our geographic footprint. We utilize LEAN continuous improvement initiatives on a company-wide basis to deliver operational excellence and improve productivity. We also extend our LEAN initiatives to customers to improve the efficiency and effectiveness of their operations and supply chains. In addition, we seek to develop a distinct competitive advantage through talent management and employee development processes and programs. We have identified certain growth engines that we believe provide substantial opportunities for above-market growth, and have developed strategies to address each of these areas of opportunity. These growth engines are a combination of business models, selected end markets and product categories, as discussed below.

Grow Our Global Account Customer Relationships and Base. Our typical global account customer is a large, multi-location industrial or commercial company, a large utility, a major contractor, or a government or institutional customer. Our global account program is designed to provide customers with supply chain management services and cost reductions by coordinating and standardizing activity for MRO materials and OEM direct materials across their multiple locations, utilizing our broad geographic footprint and our largely integrated information technology platform. Comprehensive account plans are developed and managed at the local, national and international levels to prioritize activities, identify key performance

Table of Contents

measures, and track progress against objectives. We involve our preferred suppliers early in the implementation process to contribute expertise and product knowledge to accelerate program implementation and delivery of cost savings and process improvements.

We plan to continue to expand our product and service offerings to existing global account customers, and increase our reach to serve additional customer locations. We plan on expanding our customer base by capitalizing on our industry expertise and supply chain optimization capabilities.

Extend Our Position in Integrated Supply Programs. Our integrated supply programs focus on optimizing the supply chain and replacing the traditional multi-vendor, resource-intensive procurement process with a single, outsourced, automated process. Each integrated supply program employs our product and distribution expertise to reduce the number of suppliers, total procurement costs, and administrative expenses, while meeting the customers' service needs and improving their operating controls. We believe that large customers will seek to utilize such services to consolidate and simplify their MRO and OEM supply chains.

We are expanding our position in North America as an integrated supply service provider by building upon established relationships within our large customer base and premier supplier network, and extending our services to additional customers and locations around the world. Our services are offered across all four of our end markets.

Expand Our Relationships with Construction Contractors. We support new construction, renovation and retrofit projects across a wide variety of vertical markets, including manufacturing, healthcare, education, enterprise data communications, telecommunications, energy and government infrastructure. We believe that significant cross selling opportunities exist for our electrical and communications products and expertise, and we plan to use our global account and integrated supply programs, LEAN initiatives and project management expertise to capitalize on new non-residential construction opportunities.

Expand Products and Services for Utilities. Our investor-owned, public power and utility contractor customers continue to focus on improving grid reliability and operating efficiency, while reducing costs. As a result, we anticipate opportunities from distribution grid improvement and transmission expansion projects as well as the adoption of integrated supply programs. Accordingly, we are focused on expanding our logistical and project services and supply chain management programs to increase our scope of supply on distribution grid, generation and other energy projects, including alternative energy projects.

Invest in Industrial MRO and Safety. Our sales of industrial maintenance, repair, and operating supply (MRO) materials include a broad range of electrical and non-electrical products used in the ongoing maintenance and repair of equipment used in production processes. These products are also used for facility upkeep in manufacturing, commercial, institutional, and other operations. In addition, through acquisitions, we have expanded our safety products, personal protection safety equipment, first aid supplies, and OSHA compliance categories to complement the industrial MRO product lines.

Expand International Operations. We seek to capitalize on existing and emerging international market opportunities through the expansion of our global product and service platforms. We follow large existing global customers into international markets, extending our procurement outsourcing, integrated supply programs and supplier relationships. Once established, we also seek to develop new business opportunities in these markets. We believe this strategy of working with well-developed customer and supplier relationships significantly reduces risk and provides the opportunity to establish profitable business. Our priorities are focused on global vertical markets including energy, mining and metals, manufacturing, and infrastructure, as well as key product categories such as communications and security.

Grow Our Communications Products Position. Over the last several years, there has been a convergence of electrical and data communications contractors. Our ability to provide both electrical and communications products and services lines as well as automation, electromechanical, non-electrical MRO, physical security and utility products has presented cross selling opportunities across WESCO. Communications products are in continual demand due to network upgrades, low voltage security investments, data center upgrades and increasing broadband and telecommunications usage.

Grow Lighting System and Sustainability Sales. Lighting applications are undergoing significant innovation, driven by energy efficiency and sustainability trends. We have expanded our sales team and marketing initiatives and increased our presence and customer base with the acquisition of Needham Electric Supply. We expect to continue to add product and service offerings to provide lighting and energy-saving solutions.

Pursue Strategic Acquisitions. In 2016, we acquired Atlanta Electrical Distributors, LLC, which expanded our construction end market presence in the growing Southeastern United States. Since 2010, we have made fourteen acquisitions that have helped us strengthen our product and services portfolio and increase our customer base, as well as provide an important source of talent.

We believe that the highly fragmented nature of the electrical and industrial distribution industry will continue to provide acquisition opportunities.

Table of Contents

Drive Operational Excellence. LEAN continuous improvement is a set of company-wide strategic initiatives to increase efficiency and effectiveness across the entire business enterprise, including sales, operations and administrative processes. The basic principles behind LEAN are to systematically identify and implement improvements through simplification, elimination of waste and reduction in errors. We apply LEAN in our distribution environment, and develop and deploy numerous initiatives through the Kaizen approach targeting improvements in sales, margin, warehouse operations, transportation, purchasing, working capital management and administrative processes. Our objective is to continue to implement LEAN initiatives across our business enterprise and to extend LEAN services to our customers and suppliers.

Talent Management. We seek to develop a distinct competitive advantage through talent management and employee engagement and development. We believe our ability to attract, develop and retain diverse human capital is imperative to ongoing business success. We improve workforce capability through various programs and processes that identify, recruit, develop and promote our talent base. Significant enhancements in these programs have been made over the last several years, and we expect to continue to refine and enhance these programs in the future.

Products and Services

Products

Our network of branches and distribution centers stock approximately 230,000 unique product stock keeping units and we provide customers with access to more than 1,000,000 different products. Each branch tailors its inventory to meet the needs of its local customers.

Representative product categories and associated product lines that we offer include:

General Supplies. Wiring devices, fuses, terminals, connectors, boxes, enclosures, fittings, lugs, terminations, wrap, splicing and marking equipment, tools and testers, safety, personal protection, sealants, cutting tools, adhesives, consumables, fasteners, janitorial and other MRO supplies;

Wire, Cable and Conduit. Wire, cable, raceway, metallic and non-metallic conduit;

Communications and Security. Structured cabling systems, broadband products, low voltage specialty systems, specialty wire and cable products, equipment racks and cabinets, access control, alarms, cameras, paging and voice solutions;

Electrical Distribution and Controls. Circuit breakers, transformers, switchboards, panel boards, metering products and busway products;

Lighting and Sustainability. Lamps, fixtures, ballasts and lighting control products, and

Automation, Controls and Motors. Motor control devices, drives, surge and power protection, relays, timers, pushbuttons, operator interfaces, switches, sensors, and interconnects.

The following table sets forth sales information by product category:

Year Ended December 31, (percentages based on total sales)	2016	2015	2014
General Supplies	40%	40%	40%
Wire, Cable and Conduit	14%	15%	16%
Communications and Security	15%	15%	14%
Electrical Distribution and Controls	11%	11%	11%
Lighting and Sustainability	12%	10%	10%
Automation, Controls and Motors	8%	9%	9%

We purchase products from a diverse group of more than 25,000 suppliers. In 2016, our ten largest suppliers accounted for approximately 32% of our purchases. Our largest supplier in 2016 was Eaton Corporation, accounting for approximately 11% of our purchases. No other supplier accounted for more than 5% of our total purchases.

Our supplier relationships are important to us, providing access to a wide range of products, technical training, and sales and marketing support. We have approximately 300 preferred supplier arrangements with more than 200 firms and purchase nearly 60% of our products pursuant to these arrangements. Consistent with industry practice, most of

our agreements with suppliers, including both distribution agreements and preferred supplier agreements, are terminable by either party on 60 days notice or less.

4

Table of Contents

Services

As part of our overall offering, we provide customers a comprehensive portfolio of value-added solutions within a wide range of service categories including construction, e-commerce, energy and sustainability, engineering services, production support, safety and security, supply chain optimization, training, and working capital. These solutions are designed to address our customers' business needs through:

- Technical support for operational and transactional process improvements;
- Inventory optimization programs, including just-in-time delivery and vendor managed inventory;
- Collaborative, cross-functional, cost savings teams;
- Dedicated on-site support personnel;
- Consultation on energy-efficient product upgrades, and
- Safety and product training for customer employees.

Competitive Strengths

As a leading electrical distributor in a highly fragmented North American market, we compete directly with global, national, regional and local distributors of electrical and other industrial supplies, along with buying groups formed by smaller distributors. Competition is generally based on product line breadth, product availability, service capabilities and price. We believe that our market leadership, broad product offering and value-added services, extensive distribution network and low-cost operator status provide distinct competitive advantages.

Market Leadership. Our ability to manage complex global supply chains, and multi-site facility maintenance programs and construction projects, which require special sourcing, technical advice, logistical support and locally based service, has enabled us to establish a strong presence in the competitive and fragmented North American electrical distribution market.

Broad Product Offering and Value-added Services. We provide a wide range of products, services and procurement solutions, which draw on our product knowledge, supply and logistics expertise, system capabilities and supplier relationships to enable our customers to maximize productivity, minimize waste, improve efficiencies, reduce costs and enhance safety. Our broad product offering and stable source of supply enables us to consistently meet customers' wide-ranging capital project, MRO and OEM requirements.

Extensive Distribution Network. We operate approximately 500 geographically dispersed branch locations and nine distribution centers (five in the United States and four in Canada). Our distribution centers add value for our customers, suppliers, and branches through the combination of a broad and deep selection of inventory, online ordering and next-day shipment capabilities, and central order handling and fulfillment. Our distribution center network reduces the lead time and cost of supply chain activities through its automated replenishment and warehouse management system, and provides economies of scale in purchasing, inventory management, administration and transportation. This extensive network, which would be difficult and expensive to replicate, allows us to:

- Enhance localized customer service, technical support and sales coverage;
- Tailor individual branch products and services to local customer needs, and
- Offer multi-site distribution capabilities to large customers and global accounts.

Low-Cost Operator. Our competitiveness has been enhanced by our consistent favorable operating cost position, which is based on the use of LEAN, strategically-located distribution centers, and purchasing economies of scale. As a result of these and other factors, our operating cost as a percentage of sales is one of the lowest in our industry. Our selling, general and administrative expenses as a percentage of revenues for 2016 were 14.3%.

Table of Contents

Geography

Our network of branches and distribution centers are located primarily in North America. We attribute revenues from external customers to individual countries on the basis of the point of sale. The following table sets forth information about us by geographic area:

	Net Sales		2014	Long-Lived Assets		
	Year Ended December 31,			December 31,		
	2016	2015		2016	2015	2014
(In thousands)						
United States	\$5,635,803	77%	\$5,665,962			