

EXPEDITORS INTERNATIONAL OF WASHINGTON INC
Form 10-Q
August 06, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2010

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: 0-13468

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.

(Exact name of registrant as specified in its charter)

Washington
(State or other jurisdiction of

incorporation or organization)

91-1069248
(IRS Employer

Identification Number)

1015 Third Avenue, 12th Floor, Seattle, Washington
(Address of principal executive offices)

98104
(Zip Code)

(206) 674-3400

(Registrant's telephone number, including area code)

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(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

At August 2, 2010, the number of shares outstanding of the issuer's Common Stock was 212,176,095.

PART I. FINANCIAL INFORMATION**Item 1. Financial Statements**

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.

AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

(In thousands, except share data)

(Unaudited)

| | June 30, 2010 | December 31, 2009 |
|---|---------------------|----------------------|
| Current Assets: | | |
| Cash and cash equivalents | \$ 960,300 | \$ 925,929 |
| Short-term investments | 705 | 655 |
| Accounts receivable, less allowance for doubtful accounts of \$13,391 at June 30, 2010 and \$14,235 at December 31, 2009 | 1,016,575 | 810,369 |
| Deferred Federal and state income taxes | 8,141 | 8,338 |
| Other | 36,686 | 42,539 |
| Total current assets | 2,022,407 | 1,787,830 |
| Property and equipment, less accumulated depreciation and amortization of \$264,468 at June 30, 2010 and \$264,372 at December 31, 2009 | 483,827 | 495,701 |
| Goodwill, net | 7,927 | 7,927 |
| Other intangibles, net | 4,218 | 4,938 |
| Other assets, net | 28,163 | 27,326 |
| Total assets | \$ 2,546,542 | \$ 2,323,722 |
| Current Liabilities: | | |
| Accounts payable | 659,237 | 546,675 |
| Accrued expenses, primarily salaries and related costs | 176,943 | 145,545 |
| Federal, state and foreign income taxes | 28,356 | 16,166 |
| Total current liabilities | 864,536 | 708,386 |
| Deferred Federal and state income taxes | 47,198 | 53,989 |
| Commitments and contingencies | | |
| Shareholders' Equity: | | |
| Preferred stock, none issued | 0 | 0 |
| Common stock, par value \$.01 per share | | |
| Issued and outstanding 212,018,342 shares at June 30, 2010, and 212,025,494 shares at December 31, 2009 | 2,120 | 2,120 |
| Additional paid-in capital | 6,572 | 18,265 |
| Retained earnings | 1,634,771 | 1,532,018 |
| Accumulated other comprehensive (loss) income | (17,043) | 604 |
| Total shareholders' equity | 1,626,420 | 1,553,007 |
| Noncontrolling interest | 8,388 | 8,340 |
| Total equity | 1,634,808 | 1,561,347 |

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| | | |
|------------------------------|--------------|--------------|
| Total liabilities and equity | \$ 2,546,542 | \$ 2,323,722 |
|------------------------------|--------------|--------------|

See accompanying notes to condensed consolidated financial statements.

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.

AND SUBSIDIARIES

Condensed Consolidated Statements of Earnings

(In thousands, except share data)

(Unaudited)

| | Three months ended | | Six months ended | |
|--|--------------------|------------------|-------------------|-------------------|
| | 2010 | June 30, 2009 | 2010 | June 30, 2009 |
| Revenues: | | | | |
| Airfreight services | \$ 732,881 | \$ 371,359 | \$ 1,292,264 | \$ 745,815 |
| Ocean freight and ocean services | 493,613 | 299,292 | 874,857 | 617,926 |
| Customs brokerage and other services | 290,276 | 224,709 | 550,758 | 444,304 |
| Total revenues | 1,516,770 | 895,360 | 2,717,879 | 1,808,045 |
| Operating Expenses: | | | | |
| Airfreight consolidation | 571,023 | 257,016 | 998,365 | 507,385 |
| Ocean freight consolidation | 400,729 | 218,891 | 701,819 | 457,117 |
| Customs brokerage and other services | 126,160 | 89,406 | 237,014 | 176,981 |
| Salaries and related costs | 221,105 | 189,565 | 420,953 | 376,774 |
| Rent and occupancy costs | 18,699 | 17,954 | 37,926 | 36,678 |
| Depreciation and amortization | 9,110 | 10,244 | 18,505 | 20,202 |
| Selling and promotion | 7,550 | 5,547 | 14,585 | 11,769 |
| Other | 23,898 | 19,810 | 49,675 | 42,738 |
| Total operating expenses | 1,378,274 | 808,433 | 2,478,842 | 1,629,644 |
| Operating income | 138,496 | 86,927 | 239,037 | 178,401 |
| Other Income (Expense): | | | | |
| Interest income | 1,484 | 2,433 | 3,259 | 6,039 |
| Interest expense | (151) | (64) | (238) | (79) |
| Other, net | 10,288 | 2,081 | 10,897 | 6,634 |
| Other income, net | 11,621 | 4,450 | 13,918 | 12,594 |
| Earnings before income taxes | 150,117 | 91,377 | 252,955 | 190,995 |
| Income tax expense | 59,708 | 37,563 | 101,236 | 77,812 |
| Net earnings | 90,409 | 53,814 | 151,719 | 113,183 |
| Less: net earnings (losses) attributable to the noncontrolling interest | 91 | (256) | 154 | (147) |
| Net earnings attributable to shareholders | \$ 90,318 | \$ 54,070 | \$ 151,565 | \$ 113,330 |

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| | | | | |
|---|-------------|-------------|-------------|-------------|
| Diluted earnings attributable to shareholders per share | \$.42 | \$.25 | \$.70 | \$.52 |
| Basic earnings attributable to shareholders per share | \$.43 | \$.25 | \$.71 | \$.53 |
| Dividends declared and paid per common share | \$.20 | \$.19 | \$.20 | \$.19 |
| Weighted average diluted shares outstanding | 216,460,977 | 216,653,968 | 216,576,596 | 216,519,551 |
| Weighted average basic shares outstanding | 212,332,375 | 212,116,679 | 212,262,928 | 212,108,636 |

See accompanying notes to condensed consolidated financial statements.

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.

AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

| | Three months ended | | Six months ended | |
|---|--------------------|-----------|------------------|------------|
| | June 30, 2010 | 2009 | June 30, 2010 | 2009 |
| Operating Activities: | | | | |
| Net earnings | \$ 90,409 | \$ 53,814 | \$ 151,719 | \$ 113,183 |
| Adjustments to reconcile net earnings to net cash provided by operating activities: | | | | |
| Provision for losses on accounts receivable | (618) | (1,075) | 1,825 | 1,569 |
| Deferred income tax expense (benefit) | 10,814 | (12,695) | 3,086 | (6,244) |
| Excess tax benefits from stock plans | (4,107) | (2,073) | (8,119) | (5,135) |
| Stock compensation expense | 11,003 | 11,371 | 22,201 | 18,271 |
| Depreciation and amortization | 9,110 | 10,244 | 18,505 | 20,202 |
| Gain on sale of assets | (109) | (6) | (404) | (10) |
| Other | 367 | 365 | 845 | 727 |
| Changes in operating assets and liabilities: | | | | |
| (Increase) decrease in accounts receivable | (219,602) | 60,379 | (232,567) | 214,343 |
| Decrease (increase) in other current assets | 2,947 | (1,308) | 1,136 | (1,323) |
| Increase (decrease) in accounts payable and accrued expenses | 121,941 | (20,329) | 165,110 | (100,499) |
| (Decrease) increase in income taxes payable, net | (1,609) | (13,601) | 24,332 | 2,284 |
| Net cash provided by operating activities | 20,546 | 85,086 | 147,669 | 257,368 |
| Investing Activities: | | | | |
| Decrease (increase) in short-term investments | 6 | (13) | (30) | 31 |
| Purchase of property and equipment | (8,118) | (7,166) | (15,700) | (15,822) |
| Proceeds from sale of property and equipment | 111 | 33 | 170 | 77 |
| Prepayment on long-term land lease | 0 | (7,344) | 0 | (7,344) |
| Other | (707) | (109) | (895) | (1,591) |
| Net cash used in investing activities | (8,708) | (14,599) | (16,455) | (24,649) |
| Financing Activities: | | | | |
| Proceeds from issuance of common stock | 11,020 | 8,868 | 23,240 | 17,404 |
| Repurchases of common stock | (53,649) | (23,760) | (71,668) | (42,972) |
| Excess tax benefits from stock plans | 4,107 | 2,073 | 8,119 | 5,135 |
| Dividends paid | (42,397) | (40,276) | (42,397) | (40,276) |
| Purchase of noncontrolling interest | 0 | 0 | 0 | (2,122) |
| Net cash used in financing activities | (80,919) | (53,095) | (82,706) | (62,831) |
| Effect of exchange rate changes on cash and cash equivalents | (12,267) | 14,911 | (14,137) | 5,066 |

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| | | | | |
|--|-----------|---------|---------|---------|
| (Decrease) increase in cash and cash equivalents | (81,348) | 32,303 | 34,371 | 174,954 |
| Cash and cash equivalents at beginning of period | 1,041,648 | 883,679 | 925,929 | 741,028 |

| | | | | |
|--|------------|------------|------------|------------|
| Cash and cash equivalents at end of period | \$ 960,300 | \$ 915,982 | \$ 960,300 | \$ 915,982 |
|--|------------|------------|------------|------------|

Interest and Taxes Paid:

| | | | | |
|--------------|--------|--------|--------|--------|
| Interest | \$ 152 | \$ 65 | \$ 239 | \$ 80 |
| Income taxes | 56,846 | 59,746 | 76,842 | 75,110 |

See accompanying notes to condensed consolidated financial statements.

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.

AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

Note 1. Summary of Significant Accounting Policies

A. Basis of Presentation

Expeditors International of Washington, Inc. (the Company) is a non-asset based provider of global logistics services operating through a worldwide network of offices, international service centers and exclusive or non-exclusive agents. The Company's customers include retailing and wholesaling, electronics, and manufacturing companies around the world.

The condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. As a result, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP) have been condensed or omitted. The Company believes that the disclosures made are adequate to make the information presented not misleading. The condensed consolidated financial statements reflect all adjustments, consisting of normal recurring items, which are, in the opinion of management, necessary to a fair statement of the results for the interim periods presented. These condensed consolidated financial statements should be read in conjunction with the financial statements and related notes included in the Company's Form 10-K as filed with the Securities and Exchange Commission on February 26, 2010. Certain 2009 amounts have been reclassified to conform with the 2010 presentation. All dollar amounts in the notes are presented in thousands except for share data.

All significant intercompany accounts and transactions have been eliminated in consolidation.

B. Accounts Receivable

The Company maintains an allowance for doubtful accounts, which is reviewed at least monthly for estimated losses resulting from the inability of its customers to make required payments for services and advances. Additional allowances may be necessary in the future if the ability of its customers to pay deteriorates. The Company has recorded accounts receivable allowances in the amounts of \$13,391 as of June 30, 2010 and \$14,235 as of December 31, 2009. Additions and write-offs have not been significant in the periods presented.

C. Comprehensive Income

Comprehensive income consists of net income and other gains and losses affecting equity that, under U.S. GAAP, are excluded from net income. For the Company, these consist of foreign currency translation adjustments, net of related income tax effects, and comprehensive income or loss attributable to the noncontrolling interests.

D. Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of the assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates.

E. Recent Accounting Pronouncements

In October 2009, the Financial Accounting Standards Board issued Accounting Standards Update (ASU) 2009 No. 13 Multiple-Deliverable Revenue Arrangements, which amends Accounting Standards Codification Topic 605 Revenue Recognition. This update provides amendments to the criteria for separating deliverables, measuring and allocating arrangement consideration to one or more units of accounting. This update establishes a selling price hierarchy for determining the selling price of a deliverable. ASU 2009 No. 13 is effective for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. The Company is required to and plans to adopt the provisions of this update beginning in the first quarter of 2011. The Company is currently assessing the impact of the adoption of ASU 2009 No. 13.

Note 2. Income Taxes

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The Company or one of its subsidiaries files income tax returns in the U.S. federal jurisdiction and various state, local and foreign jurisdictions. The Company is no longer subject to U.S. federal income tax examinations by tax authorities for years prior to 2006. With respect to state and local jurisdictions and countries outside of the United States, with limited exceptions, the Company and its subsidiaries are no longer subject to income tax audits for years prior to 2001. In the normal course of business, the Company is subject to examination by taxing authorities throughout the world. Although the outcome of tax audits is always uncertain, the Company believes that adequate amounts of tax, interest and penalties have been provided for any adjustments that may result from these open tax years.

Any interest and penalties expensed in relation to the underpayment of income taxes were insignificant for the three and six months ended June 30, 2010 and 2009. Based on management's review of the Company's tax positions, the Company had no significant unrecognized tax benefits as of June 30, 2010 and December 31, 2009.

Note 3. Share Based Compensation

The Company provides compensation benefits by granting stock options and employee stock purchase rights to its employees and restricted shares to its directors. On May 5, 2010, the shareholders approved the Company's 2010 Stock Option Plan (2010 Plan), which made available a total of 3,000,000 shares of the Company's common stock for purchase upon exercise of options granted under the 2010 Plan. The Company's annual grant of option awards and restricted shares generally takes place during the second quarter of each fiscal year. For the six-month periods ended June 30, 2010 and 2009, 2,634,885 and 2,446,400 options were granted, respectively. Also, for the six months ended June 30, 2010 and 2009, 26,735 and 29,230 shares were granted to non-employee directors under the 2008 Directors' Restricted Stock Plan. The grant of employee stock purchase rights and the issuance of shares under the employee stock purchase plan are made in the third quarter of each fiscal year and none were issued in the three and six-month periods ended June 30, 2010 and 2009.

The Company recognizes compensation expense based on the estimated fair value of options awarded under its stock option and employee stock purchase rights plans. The stock compensation expense, adjusted for expected forfeitures, is recognized on a straight-line basis over the vesting period. The forfeiture assumption used to calculate compensation expense is primarily based on historical pre-vesting employee forfeiture patterns. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions:

| | Six months ended June 30, | |
|--|------------------------------|-------------|
| | 2010 | 2009 |
| Dividend yield | 1.08% | 1.25% |
| Volatility - stock option plans | 38 - 40% | 38 - 39% |
| Risk-free interest rates | 2.18 - 2.86% | 2.81% |
| Expected life (years) - stock option plans | 5.44 - 6.90 | 6.09 - 7.86 |
| Weighted average fair value of stock options granted during the period | \$ 14.51 | \$ 13.84 |

The compensation expense for restricted stock awards is based on the fair market value of the Company's share of common stock on the date of grant. On June 1, 2010 and June 1, 2009, restricted shares were granted with a fair value per share of \$37.40 and \$34.21, respectively.

Total stock compensation expense and the total related tax benefit are recognized as follows:

| | Three months ended June 30, | | Six months ended June 30, | |
|----------------------------|--------------------------------|-----------|------------------------------|-----------|
| | 2010 | 2009 | 2010 | 2009 |
| Stock compensation expense | \$ 11,003 | \$ 11,371 | \$ 22,201 | \$ 18,271 |
| Recognized tax benefit | \$ 52 | \$ 71 | \$ 109 | \$ 148 |

Note 4. Basic and Diluted Earnings per Share

The following table reconciles the numerator and the denominator of the basic and diluted per share computations for earnings attributable to shareholders per share:

| (Amounts in thousands, except share and per share amounts) | Net Earnings Attributable to Shareholders | Three months ended June 30, | |
|--|---|-----------------------------|--------------------|
| | | Weighted Average Shares | Earnings Per Share |
| 2010 | | | |
| Basic earnings attributable to shareholders | \$ 90,318 | 212,332,375 | \$.43 |
| Effect of dilutive potential common shares | | 4,128,602 | |

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| | | | | |
|--|-----------|-------------|----|-----|
| Dilutive earnings attributable to shareholders | \$ 90,318 | 216,460,977 | \$ | .42 |
| <u>2009</u> | | | | |
| Basic earnings attributable to shareholders | \$ 54,070 | 212,116,679 | \$ | .25 |
| Effect of dilutive potential common shares | | 4,537,289 | | |
| Dilutive earnings attributable to shareholders | \$ 54,070 | 216,653,968 | \$ | .25 |

| (Amounts in thousands, except share and per share amounts) | Six months ended June 30, | | |
|--|---|----------------------------|--------------------|
| | Net Earnings Attributable to Shareholders | Weighted Average Shares | Earnings Per Share |
| 2010 | | | |
| Basic earnings attributable to shareholders | \$ 151,565 | 212,262,928 | \$.71 |
| Effect of dilutive potential common shares | | 4,313,668 | |
| Dilutive earnings attributable to shareholders | \$ 151,565 | 216,576,596 | \$.70 |
| 2009 | | | |
| Basic earnings attributable to shareholders | \$ 113,330 | 212,108,636 | \$.53 |
| Effect of dilutive potential common shares | | 4,410,915 | |
| Dilutive earnings attributable to shareholders | \$ 113,330 | 216,519,551 | \$.52 |

The following shares have been excluded from the computation of diluted earnings per share because the effect would have been antidilutive:

| | Three months ended June 30, | | Six months ended June 30, | |
|--------|--------------------------------|-----------|------------------------------|-----------|
| | 2010 | 2009 | 2010 | 2009 |
| Shares | 11,114,502 | 8,928,830 | 11,114,502 | 8,931,630 |

Note 5. Components of Equity and Comprehensive Income

The components of equity for the six months ended June 30, 2010 and 2009 are as follows:

| | Shareholders equity | Noncontrolling interest | Total equity |
|---|------------------------|----------------------------|-----------------|
| Balance at December 31, 2009 | \$ 1,553,007 | 8,340 | 1,561,347 |
| Exercise of stock options | 23,240 | | 23,240 |
| Shares repurchased under provisions of stock repurchase plans | (71,668) | | (71,668) |
| Stock compensation expense | 22,201 | | 22,201 |
| Tax benefits from stock plans | 8,119 | | 8,119 |
| Comprehensive Income | | | |
| Net earnings | 151,565 | 154 | 151,719 |
| Foreign currency translation adjustments, net of tax of \$9,681 | (17,647) | (106) | (17,753) |
| Total comprehensive income | 133,918 | 48 | 133,966 |
| Dividends paid (\$.20 per share) | (42,397) | | (42,397) |
| Balance at June 30, 2010 | \$ 1,626,420 | 8,388 | 1,634,808 |
| Balance at December 31, 2008 | \$ 1,366,418 | 17,498 | 1,383,916 |
| Exercise of stock options | 17,404 | | 17,404 |
| Shares repurchased under provisions of stock repurchase plans | (42,972) | | (42,972) |
| Stock compensation expense | 18,271 | | 18,271 |
| Tax benefits from stock plans | 5,135 | | 5,135 |
| Purchase of noncontrolling interest | (281) | (186) | (467) |
| Comprehensive Income | | | |
| Net earnings | 113,330 | (147) | 113,183 |
| Foreign currency translation adjustments, net of tax of \$4,684 | 8,539 | 8 | 8,547 |

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| | | | |
|---|---------------------|--------------|------------------|
| Total comprehensive income | 121,869 | (139) | 121,730 |
| Dividends paid (\$.19 per share) | (40,276) | | (40,276) |
| Distributions or declaration of dividends to noncontrolling interest ⁽¹⁾ | | (8,058) | (8,058) |
| Balance at June 30, 2009 | \$ 1,445,568 | 9,115 | 1,454,683 |

⁽¹⁾ Amount of earnings owed to the noncontrolling interest at the time their ownership interest was purchased. These earnings, reclassified from noncontrolling interest to accounts payable, were distributed in periods subsequent to the effective date of the purchase, including \$1,655 paid during the six months ended June 30, 2009.

The components of total comprehensive income for interim periods are as follows:

| (in thousands) | Three months ended June 30, | | Six months ended June 30, | |
|---|--------------------------------|-----------|------------------------------|------------|
| | 2010 | 2009 | 2010 | 2009 |
| Net earnings | \$ 90,409 | \$ 53,814 | \$ 151,719 | \$ 113,183 |
| Foreign currency translation adjustments, net of tax of \$7,970 and \$10,989 for the three months ended June 30, 2010 and 2009, and \$9,681 and \$4,684 for the six months ended June 30, 2010 and 2009 | (14,621) | 20,059 | (17,753) | 8,547 |
| Comprehensive income | 75,788 | 73,873 | 133,966 | 121,730 |
| Less: comprehensive (loss) income attributable to the noncontrolling interest | (1) | (232) | 48 | (139) |
| Comprehensive income attributable to shareholders | \$ 75,789 | \$ 74,105 | \$ 133,918 | \$ 121,869 |

On May 5, 2010, the Board of Directors declared a semi-annual cash dividend of \$.20 per share payable on June 15, 2010 to shareholders of record as of June 1, 2010.

On May 7, 2009, the Board of Directors declared a semi-annual cash dividend of \$.19 per share payable on June 15, 2009 to shareholders of record as of June 1, 2009.

Note 6. Fair Value of Financial Instruments

The Company's financial instruments, other than cash, consist primarily of cash equivalents, short-term investments, accounts receivable, accounts payable and accrued expenses. The carrying value of these financial instruments approximates their fair value. Cash equivalents consist of highly liquid investments with a maturity of three months or less at date of purchase. Short term investments have a maturity of greater than three months at date of purchase. Cash, cash equivalents and short-term investments consist of the following: