

CARBO CERAMICS INC  
Form 10-Q  
August 01, 2012  
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# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

## FORM 10-Q

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

For the quarterly period ended June 30, 2012

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 No. 001-15903

# CARBO CERAMICS INC.

(Exact name of registrant as specified in its charter)

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**DELAWARE**  
(State or other jurisdiction of

**72-1100013**  
(I.R.S. Employer

incorporation or organization)

Identification Number)

**575 North Dairy Ashford**

**Suite 300**

**Houston, TX 77079**

(Address of principal executive offices)

**(281) 921-6400**

(Registrant's telephone number)

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.

Large accelerated filer ☒

Accelerated filer ☐

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

Smaller reporting company ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

As of July 31, 2012, 23,084,166 shares of the registrant's Common Stock, par value \$.01 per share, were outstanding.

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**CARBO CERAMICS INC.**

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## PART I. FINANCIAL INFORMATION

**ITEM 1. FINANCIAL STATEMENTS****CARBO CERAMICS INC.****CONSOLIDATED BALANCE SHEETS**

(\$ in thousands, except per share data)

	<b>June 30, 2012 (Unaudited)</b>	<b>December 31, 2011 (Note 1)</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 34,866	\$ 41,270
Trade accounts and other receivables, net	117,337	112,014
Inventories:		
Finished goods	101,173	105,233
Raw materials and supplies	28,965	26,783
Total inventories	130,138	132,016
Prepaid expenses and other current assets	5,488	4,023
Prepaid income taxes		3,279
Deferred income taxes	9,909	9,963
Total current assets	297,738	302,565
Property, plant and equipment:		
Land and land improvements	14,510	14,512
Land-use and mineral rights	7,618	8,610
Buildings	70,798	67,120
Machinery and equipment	493,378	455,563
Construction in progress	55,119	48,778
Total	641,423	594,583
Less accumulated depreciation and amortization	220,673	201,924
Net property, plant and equipment	420,750	392,659
Goodwill	12,164	12,164
Intangible and other assets, net	32,624	33,477
Total assets	\$ 763,276	\$ 740,865
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 20,101	\$ 38,192
Accrued income taxes	1,233	
Other accrued expenses	28,392	40,874
Total current liabilities	49,726	79,066
Deferred income taxes	36,476	31,641
Shareholders' equity:		
Preferred stock, par value \$0.01 per share, 5,000 shares authorized, none outstanding		

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Common stock, par value \$0.01 per share, 80,000,000 and 40,000,000 shares authorized at June 30, 2012 and December 31, 2011, respectively; 23,084,828 and 23,106,358 shares issued and outstanding at June 30, 2012 and December 31, 2011, respectively

	231	231
Additional paid-in capital	55,032	56,539
Retained earnings	626,437	577,253
Accumulated other comprehensive loss	(4,626)	(3,865)
 Total shareholders' equity	 677,074	 630,158
 Total liabilities and shareholders' equity	 \$ 763,276	 \$ 740,865

The accompanying notes are an integral part of these statements.

**Table of Contents****CARBO CERAMICS INC.****CONSOLIDATED STATEMENTS OF INCOME**

(\$ in thousands, except per share data)

(Unaudited)

	<b>Three months ended June 30,</b>		<b>Six months ended June 30,</b>	
	<b>2012</b>	<b>2011</b>	<b>2012</b>	<b>2011</b>
Revenues	\$ 177,614	\$ 149,669	\$ 340,780	\$ 300,499
Cost of sales	113,361	87,551	213,063	176,325
Gross profit	64,253	62,118	127,717	124,174
Selling, general and administrative expenses	17,056	15,845	33,708	30,132
Start-up costs	6		68	
(Gain) loss on disposal or impairment of assets	(59)	(30)	(54)	1,649
Operating profit	47,250	46,303	93,995	92,393
Other income (expense):				
Interest income (expense), net	9	56	(35)	100
Foreign currency exchange gain (loss), net	579	(126)	144	(314)
Other, net	47	(53)	(212)	(130)
	635	(123)	(103)	(344)
Income before income taxes	47,885	46,180	93,892	92,049
Income taxes	15,968	16,236	31,684	31,941
Net income	\$ 31,917	\$ 29,944	\$ 62,208	\$ 60,108
Earnings per share:				
Basic	\$ 1.38	\$ 1.29	\$ 2.69	\$ 2.60
Diluted	\$ 1.38	\$ 1.29	\$ 2.69	\$ 2.60
Other information:				
Dividends declared per common share (See Note 4)	\$	\$	\$ 0.48	\$ 0.40

The accompanying notes are an integral part of these statements.

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**CARBO CERAMICS INC.**

**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

(\$ in thousands)

(Unaudited)

	<b>Three months ended June 30,</b>		<b>Six months ended June 30,</b>	
	<b>2012</b>	<b>2011</b>	<b>2012</b>	<b>2011</b>
Net income	\$ 31,917	\$ 29,944	\$ 62,208	\$ 60,108
Other comprehensive (loss) income:				
Foreign currency translation adjustment	(6,002)	1,436	(1,171)	5,251
Deferred income tax benefit (expense)	2,101	(591)	410	(810)
Other comprehensive (loss) income, net of tax	(3,901)	845	(761)	4,441
Comprehensive income	\$ 28,016	\$ 30,789	\$ 61,447	\$ 64,549

The accompanying notes are an integral part of these statements.

**Table of Contents****CARBO CERAMICS INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS**

(\$ in thousands)

(Unaudited)

	<b>Six months ended June 30,</b>	
	<b>2012</b>	<b>2011</b>
<b>Operating activities</b>		
Net income	\$ 62,208	\$ 60,108
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	21,801	16,487
Provision for doubtful accounts	12	
Deferred income taxes	5,299	2,905
Excess tax benefits from stock based compensation	(1,257)	(1,270)
(Gain)/loss on disposal or impairment of assets	(54)	1,649
Foreign currency transaction (gain) loss, net	(144)	314
Stock compensation expense	3,087	2,795
Changes in operating assets and liabilities:		
Trade accounts and other receivables	(5,525)	(14,291)
Inventories	1,938	(13,293)
Prepaid expenses and other current assets	(1,451)	(2,242)
Long-term prepaid expenses	766	447
Accounts payable	(18,142)	(2,583)
Accrued expenses	(12,482)	2,689
Accrued income taxes, net	5,764	(1,576)
<b>Net cash provided by operating activities</b>	<b>61,820</b>	<b>52,139</b>
<b>Investing activities</b>		
Capital expenditures	(50,288)	(37,468)
<b>Net cash used in investing activities</b>	<b>(50,288)</b>	<b>(37,468)</b>
<b>Financing activities</b>		
Proceeds from bank borrowings	10,000	
Repayments on bank borrowings	(10,000)	
Net proceeds from stock based compensation		76
Dividends paid	(11,095)	(9,264)
Purchase of common stock	(7,655)	(814)
Excess tax benefits from stock based compensation	1,257	1,270
<b>Net cash used in financing activities</b>	<b>(17,493)</b>	<b>(8,732)</b>
<b>Effect of exchange rate changes on cash</b>	<b>(443)</b>	<b>655</b>
<b>Net (decrease) increase in cash and cash equivalents</b>	<b>(6,404)</b>	<b>6,594</b>
<b>Cash and cash equivalents at beginning of period</b>	<b>41,270</b>	<b>46,656</b>
<b>Cash and cash equivalents at end of period</b>	<b>\$ 34,866</b>	<b>\$ 53,250</b>

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### Supplemental cash flow information

Interest paid	\$	72	\$
Income taxes paid	\$	20,621	\$ 30,611

The accompanying notes are an integral part of these statements.

**Table of Contents****CARBO CERAMICS INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(\$ in thousands, except per share data)

(Unaudited)

**1. Basis of Presentation**

The accompanying unaudited consolidated financial statements of CARBO Ceramics Inc. have been prepared in accordance with United States generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required for complete financial statements. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, considered necessary for a fair presentation have been included. The results of the interim periods presented herein are not necessarily indicative of the results to be expected for any other interim period or the full year. The consolidated balance sheet as of December 31, 2011 has been derived from the audited financial statements at that date. These financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto for the year ended December 31, 2011 included in the annual report on Form 10-K of CARBO Ceramics Inc. for the year ended December 31, 2011.

The consolidated financial statements include the accounts of CARBO Ceramics Inc. and its operating subsidiaries (the Company). All significant intercompany transactions have been eliminated.

*Cash Equivalents*

The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. The carrying amounts reported in the balance sheet for cash equivalents approximate fair value.

*Disposal or Impairment of Assets*

During the three month period ended March 31, 2011, the Company recorded an \$890 impairment of goodwill related to the Company's geotechnical monitoring business and a \$760 write-down of a 6% interest in an investment accounted for under the cost method, as a result of the sale of the business by majority shareholders.

**2. Earnings Per Share**

The following table sets forth the computation of basic and diluted earnings per share under the two-class method:

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
<b>Numerator for basic and diluted earnings per share:</b>				
Net income	\$ 31,917	\$ 29,944	\$ 62,208	\$ 60,108
Effect of reallocating undistributed earnings of participating securities	(171)	(174)	(336)	(350)
Net income available under the two-class method	\$ 31,746	\$ 29,770	\$ 61,872	\$ 59,758
<b>Denominator:</b>				
Denominator for basic earnings per share weighted-average shares	22,961,130	23,027,104	22,967,558	23,020,851
Effect of dilutive securities:				
Employee stock options	1,220	1,346	1,250	1,324

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Dilutive potential common shares	1,220	1,346	1,250	1,324
Denominator for diluted earnings per share adjusted weighted-average shares	22,962,350	23,028,450	22,968,808	23,022,175
Basic earnings per share	\$ 1.38	\$ 1.29	\$ 2.69	\$ 2.60
Diluted earnings per share	\$ 1.38	\$ 1.29	\$ 2.69	\$ 2.60

**Table of Contents****3. Common Stock Repurchase Program**

On August 28, 2008, the Company's Board of Directors authorized the repurchase of up to two million shares of the Company's Common Stock. Shares are effectively retired at the time of purchase. During the six months ended June 30, 2012, the Company repurchased and retired 60,000 shares at an aggregate price of \$5,726. As of June 30, 2012, the Company has repurchased and retired 1,877,576 shares at an aggregate price of \$78,301.

**4. Dividends Paid**

On March 20, 2012, the Board of Directors declared a cash dividend of \$0.24 per common share payable to shareholders of record on May 1, 2012. The dividend was paid on May 15, 2012. On July 17, 2012, the Board of Directors declared a cash dividend of \$0.27 per common share payable to shareholders of record on August 1, 2012. This dividend is payable on August 15, 2012.

**5. Stock Based Compensation**

The CARBO Ceramics Inc. Omnibus Incentive Plan (the "Omnibus Incentive Plan") provides for granting of cash-based awards, stock options (both non-qualified and incentive) and other equity-based awards (including stock appreciation rights, phantom stock, restricted stock, restricted stock units, performance shares, deferred share units or share-denominated performance units) to employees and non-employee directors. The amount paid under the Omnibus Incentive Plan to any single participant in any calendar year with respect to any cash-based award shall not exceed \$2,000. Awards may be granted with respect to a number of shares of the Company's Common Stock that in the aggregate does not exceed 750,000 shares prior to the fifth anniversary of its effective date, plus (i) the number of shares that are forfeited, cancelled or returned, and (ii) the number of shares that are withheld from the participants to satisfy an option exercise price or minimum statutory tax withholding obligations. No more than 50,000 shares may be granted to any single participant in any calendar year. Equity-based awards may be subject to performance-based and/or service-based conditions. With respect to stock options and stock appreciation rights granted, the exercise price shall not be less than the market value of the underlying Common Stock on the date of grant. The maximum term of an option is ten years. Restricted stock awards granted generally vest (i.e., transfer and forfeiture restrictions on these shares are lifted) in equal annual installments over a three-year period but subject to certain limitations, awards may specify other vesting periods. As of June 30, 2012, 569,091 shares were available for issuance under the Omnibus Incentive Plan. Although the Company's previous stock option plan has expired, outstanding options under the plan remain outstanding in accordance with their terms.

As of June 30, 2012, all compensation cost related to stock options granted under the expired stock option plan has been recognized. There were no stock options exercised during the six months ended June 30, 2012. The weighted-average remaining contractual term of the 2,425 options outstanding at June 30, 2012 was approximately 3 months.

A summary of restricted stock activity and related information for the six months ended June 30, 2012 is presented below:

	Shares	Weighted-Average Grant-Date Fair Value
Nonvested at January 1, 2012	129,082	\$ 75.00
Granted	55,652	\$ 119.22
Vested	(58,461)	\$ 66.15
Forfeited	(3,946)	\$ 93.80
Nonvested at June 30, 2012	122,327	\$ 98.75

As of June 30, 2012, there was \$7,944 of total unrecognized compensation cost, net of estimated forfeitures, related to restricted shares granted under the Omnibus Incentive Plan. That cost is expected to be recognized over a weighted-average period of 1.7 years. The total fair value of shares vested during the six months ended June 30, 2012 was \$3,867.

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The Company has made phantom stock awards to key international employees pursuant to the Omnibus Incentive Plan. The units subject to an award vest and cease to be forfeitable in equal annual installments over a three-year period. Participants awarded units of phantom shares are entitled to a lump sum cash payment equal to the fair market value of a share of Common Stock on the vesting date. In no event will Common Stock of the Company be issued with regard to outstanding phantom shares. As of June 30, 2012, there were 10,105 units of phantom shares granted under the Omnibus Incentive Plan, of which 3,429 have vested and 1,076 have been forfeited, with a total value of \$430, a portion of which is accrued as a liability within Other Accrued Expenses.

### **6. Bank Borrowings**

The Company has an unsecured revolving credit agreement with a bank. On March 5, 2012, the Company entered into a first amendment to this credit agreement to (i) extend its maturity date from January 29, 2013 to July 29, 2013, (ii) increase the size from \$10,000 to \$25,000, and (iii) make other administrative changes to certain covenants and provisions. The Company has the option of choosing either the bank's fluctuating Base Rate or LIBOR Fixed Rate, plus an Applicable Margin, all as defined in the credit agreement. The terms of the credit agreement provide for certain affirmative and negative covenants and require the Company to maintain certain financial ratios. Commitment fees are payable quarterly at the annual rate of 0.50% of the unused line of credit. During the six-month period ended June 30, 2012, the Company borrowed and repaid \$10,000 under the line of credit.

### **7. Foreign Currencies**

As of June 30, 2012, the Company's net investment that is subject to foreign currency fluctuations totaled \$86,816 and the Company has recorded cumulative foreign currency translation loss of \$4,626, net of deferred income tax benefit. This cumulative translation loss is included in Accumulated Other Comprehensive Loss.

### **8. New Accounting Pronouncements**

In December 2010, the FASB issued authoritative guidance on application of the goodwill impairment model when a reporting unit has a zero or negative carrying amount. When a reporting unit has a zero or negative carrying value, Step 2 of the goodwill impairment test should be performed if qualitative factors indicate that it is more likely than not that a goodwill impairment exists. The guidance is effective for the Company beginning in the first quarter of fiscal 2012. The Company adopted this guidance as of January 1, 2012. The adoption did not have a material impact on the Company's financial position, results of operations or cash flows.

In December 2010, the FASB issued authoritative guidance on disclosure of supplementary pro forma information for business combinations. The new guidance requires that pro forma financial information should be prepared as if the business combination occurred as of the beginning of the prior annual period. The guidance is effective for the Company for business combinations with acquisition dates occurring in and from the first quarter of fiscal 2012. The Company adopted this guidance as of January 1, 2012. The adoption did not have a material impact on the Company's financial position, results of operations or cash flows.

### **9. Legal Proceedings**

The Company is subject to legal proceedings, claims and litigation arising in the ordinary course of business. While the outcome of these matters is currently not determinable, management does not expect that the ultimate costs to resolve these matters will have a material adverse effect on the Company's consolidated financial position, results of operations, or cash flows.

On February 9, 2012, the Company and two of its officers, Gary A. Kolstad and Ernesto Bautista III, were named as defendants in a purported class-action lawsuit filed in the United States District Court for the Southern District of New York (the "February SDNY Lawsuit"), brought on behalf of shareholders who purchased the Company's Common Stock between October 27, 2011 and January 26, 2012 (the "Relevant Time Period"). The suit alleges violations of the federal securities laws arising from statements concerning the Company's business operations and business prospects that were made during the Relevant Time Period and requests unspecified damages and costs. On April 10, 2012, a second purported class-action lawsuit was filed against the same defendants in the United States District Court for the Southern District of New York, brought

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on behalf of shareholders who purchased or sold CARBO Ceramics Inc. option contracts during the Relevant Time Period (the April SDNY Lawsuit, and collectively with the February SDNY Lawsuit, the Federal Securities Lawsuit ), which alleges substantially similar claims as the February SDNY Lawsuit and requests unspecified damages and costs. In June 2012, the February SDNY Lawsuit and the April SDNY Lawsuit were consolidated, and will now proceed as one lawsuit.

On April 19, 2012, a third purported class-action lawsuit was filed against the same defendants in the United States District Court for the Southern District of Texas, which was also brought on behalf of shareholders who purchased shares during the Relevant Time Period. This lawsuit alleged substantially similar claims as the February SDNY Lawsuit and requested unspecified damages and costs. In June 2012, this lawsuit was dismissed without prejudice.

On March 1, 2012, the Directors of the Company and Mr. Bautista were named as defendants in a purported derivative action lawsuit brought on behalf of the Company by a stockholder in District Court in Harris County, Texas (the March Harris County Lawsuit ). The suit alleges various breaches of fiduciary duty and other duties by the defendants that generally are related to the February SDNY Lawsuit, and requests unspecified damages and costs. The parties to this lawsuit have entered into an agreement to stay further proceedings pending the outcome of a motion to dismiss the Federal Securities Lawsuit.

On June 13, 2012, the Directors of the Company and Mr. Bautista were named as defendants in a second purported derivative action lawsuit brought on behalf of the Company by a stockholder in District Court in Harris County, Texas (this lawsuit collectively with the March Harris County Lawsuit, the Harris County Lawsuits ). This lawsuit alleges substantially similar claims as the March Harris County Lawsuit as well as a breach of duty against certain defendants in connection with stock sales. This lawsuit also requests unspecified damages and costs. The parties to this lawsuit have also entered into an agreement to stay further proceedings pending the outcome of a motion to dismiss the Federal Securities Lawsuit.

While each of the Federal Securities Lawsuit and the Harris County Lawsuits are in their preliminary stages, the Company does not believe they have merit, and plans to vigorously contest and defend against them.

The Company cannot predict the ultimate outcome or duration of these lawsuits.

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### **ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

#### **Business**

The Company generates revenue primarily through the sale of products and services to the oil and natural gas industry. The Company's principal business consists of manufacturing and selling ceramic proppant and resin-coated sand for use primarily in the hydraulic fracturing of oil and natural gas wells. The Company also provides the industry's most popular hydraulic fracture simulation software FracPro®, as well as hydraulic fracture design and consulting services. In addition, the Company provides a broad range of technologies for spill prevention, containment and countermeasures, along with geotechnical monitoring.

#### **Critical Accounting Policies**

The consolidated financial statements are prepared in accordance with United States generally accepted accounting principles, which require the Company to make estimates and assumptions (see Note 1 to the consolidated financial statements included in the annual report on Form 10-K for the year ended December 31, 2011). The Company believes that some of its accounting policies involve a higher degree of judgment and complexity than others. As of December 31, 2011, critical accounting policies for the Company included revenue recognition, estimating the recoverability of accounts receivable, inventory valuation, accounting for income taxes and accounting for long-lived assets. These critical accounting policies are discussed more fully in the Company's annual report on Form 10-K for the year ended December 31, 2011. There have been no changes in the Company's evaluation of its critical accounting policies since December 31, 2011.

#### **Results of Operations**

##### **Three Months Ended June 30, 2012**

*Revenues.* Revenues of \$177.6 million for the quarter ended June 30, 2012 increased 19% compared to \$149.7 million in revenues for the same period in 2011. The increase is mainly attributed to a 17% increase in proppant sales volume and an increase in revenues of some of the Company's other business units. Worldwide proppant sales volume totaled 454 million pounds for the second quarter of 2012 compared to 387 million pounds for the second quarter of 2011. North American (defined as Canada and the U.S.) sales volume increased 17% largely driven by an increase in the oil rig count in the U.S. as well as acceptance of the Company's products in oily, liquids-rich basins. International (excluding Canada) sales volume increased 20% primarily due to increased sales volumes in Mexico and Russia. Other Proppants (resin-coated sand and ceramic proppant manufactured on an outsourced basis) represented 51 million pounds of the Company's worldwide sales volumes in the second quarter of 2012, as compared to 23 million pounds in the second quarter of 2011. The average selling price per pound of all proppant remained relatively flat at \$0.358 during the second quarter of 2012 compared to \$0.356 for the same period in 2011.

*Gross Profit.* Gross profit for the second quarter of 2012 was \$64.3 million, or 36% of revenues, compared to \$62.1 million, or 42% of revenues, for the second quarter of 2011. The increase in gross profit was primarily the result of higher proppant sales volumes and a greater contribution from some of the Company's other business units, partially offset by an increase in freight and logistics costs. Gross profit as a percentage of revenues decreased primarily as a result of higher freight and logistics costs and a change in the mix of products sold.

*Selling, General and Administrative (SG&A).* SG&A expenses totaled \$17.1 million for the second quarter of 2012 compared to \$15.8 million for the same period in 2011. As a percentage of revenues, SG&A expenses decreased to 9.6% compared to 10.6% for the second quarter of 2011.

*Other Income (Expense).* Other income for the second quarter of 2012 increased \$0.8 million compared to the same period in 2011. This increase is mainly attributed to gains resulting from changes in exchange rates between the functional currency and the foreign currency in which the effective transactions were denominated.

*Income Tax Expense.* Income tax expense was \$16.0 million, or 33.3% of pretax income, for the second quarter of 2012 compared to \$16.2 million, or 35.2% of pretax income, for the same period last year. The lower effective tax rate is primarily due to additional tax benefits relating to mining depletion deductions.

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### **Six Months Ended June 30, 2012**

*Revenues.* Revenues of \$340.8 million for the six months ended June 30, 2012 increased 13% compared to \$300.5 million in revenues for the same period in 2011. Revenues increased primarily due to a 9% increase in proppant sales volume, a 3% increase in the average proppant selling price and an increase in revenues for some of the Company's other business units. Worldwide proppant sales volume totaled 857 million pounds in the first six months of 2012 compared to 785 million pounds for the same period in 2011. North American (defined as Canada and the U.S.) sales volume increased 7% due primarily to an increase in the oil rig count in the U.S. as well as acceptance of the Company's products in oily, liquids-rich basins. International (excluding Canada) sales volume increased 21% primarily due to increased sales volumes in Mexico, Russia and China. Other Proppants (resin-coated sand and ceramic proppant manufactured on an outsourced basis) represented 92 million pounds of the Company's worldwide sales volumes in the first six months of 2012, as compared to 46 million pounds for the same period in 2011. The average selling price per pound of all proppant was \$0.364 during the six months ended June 30, 2012 compared to \$0.353 for the same period in 2011.

*Gross Profit.* Gross profit for the six months ended June 30, 2012 was \$127.7 million, or 37% of revenues, compared to \$124.2 million, or 41% of revenues, for the same period in 2011. The increase in gross profit was primarily the result of higher proppant sales volumes, an increase in the average proppant selling price and a greater contribution from some of the Company's other business units, partially offset by an increase in freight and logistics costs. Gross profit as a percentage of revenues decreased primarily as a result of higher freight and logistics costs and a change in the mix of products sold.

*Selling, General and Administrative (SG&A) and Other Operating Expenses.* SG&A expenses totaled \$33.7 million for the six months ended June 30, 2012 compared to \$30.1 million for the same period in 2011. As a percentage of revenues, SG&A expenses remained relatively flat at 9.9% for the six months ended June 30, 2012 compared to 10.0% for the same period in 2011. The increase in SG&A expenses primarily resulted from higher marketing, research and development, and administrative spending. Start-up costs of \$0.1 million in 2012 related to the start-up of the second resin-coating line at the Company's New Iberia, Louisiana facility. Loss on disposal or impairment of assets of \$1.6 million in 2011 consists primarily of a \$0.9 million impairment of goodwill related to the Company's geotechnical monitoring business and a \$0.8 million write-down of a 6% interest in an investment accounted for under the cost method as a result of the sale of the business by majority shareholders.

*Other Income (Expense).* Other expense for the six months ended June 30, 2012 decreased \$0.2 million compared to the same period in 2011 due primarily to changes in exchange rates between the functional currency and the foreign currency in which the effective transactions were denominated.

*Income Tax Expense.* Income tax expense was \$31.7 million, or 33.7% of pretax income, for the six months ended June 30, 2012 compared to \$31.9 million, or 34.7% of pretax income for the same period last year. The lower effective tax rate is due primarily to additional tax benefits in 2012 relating to mining depletion deductions.

## **Outlook**

The Company believes its operating results for the remainder of 2012 will continue to be influenced by the level of oil and natural gas drilling in North America. A severe decline in natural gas prices in the U.S. in late 2011 led businesses engaged in the exploration and production of oil and natural gas to reduce drilling activity and capital spending in natural gas basins, including shale plays, and to increase capital spending towards oily, liquids-rich basins.

The continuing shift in oilfield activity by the Company's clients to oily, liquids-rich plays remains encouraging. However, the combination of a low natural gas price, volatility in oil and natural gas liquids markets, and the over-supply of imported Chinese ceramic proppant is causing disruptions within the industry, and the Company believes these disruptions will place pressure on proppant pricing, volumes and margins for the remainder of the year. In addition, the increased amount of activity in infrastructure-limited, liquids-rich basins introduced supply chain challenges to the industry. These challenges resulted in higher supply chain costs in the first half of 2012 for the Company. The Company expects that a portion of these costs will likely continue for the balance of the year.

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The Company expects to support near-term demand with its current ceramic production capacity of 1.7 billion pounds per year, along with existing inventories of ceramic proppant that meets API/ISO standards manufactured on an outsourced basis. With respect to resin-coating capacity expansion, the second production line in New Iberia, Louisiana was completed during the first quarter of 2012 and increased the Company's annual resin-coating capacity to 400 million pounds. Near the end of the second quarter of 2012, the Company began to utilize its own northern white sand in its sand processing facility in Marshfield, Wisconsin. With respect to the resin-coating expansion in Marshfield, the Company has deferred further construction at this time. The Company will consider resuming construction when warranted by market conditions. Additionally, the Company has been issued an Air Quality Permit for its proposed ceramic proppant manufacturing plant in Millen, Georgia. The Company is moving forward with construction of the first 250 million pound line and anticipates the Millen plant could commence operation before the end of 2013.

## **Liquidity and Capital Resources**

At June 30, 2012, the Company had cash and cash equivalents of \$34.9 million compared to cash and cash equivalents of \$41.3 million at December 31, 2011. For the six months ended June 30, 2012, the Company generated \$61.8 million of cash from operating activities and \$1.3 million from excess tax benefits relating to stock based compensation. Uses of cash included \$50.3 million of capital spending, \$11.1 million of cash dividends, \$7.7 million for the repurchases of the Company's Common Stock and \$0.4 million for the effect of exchange rate changes on cash. In addition, during the first six months of 2012, the Company borrowed and fully repaid a total of \$10.0 million on its credit facility.

Subject to the Company's financial condition, the amount of funds generated from operations and the level of capital expenditures, the Company's current intention is to continue to pay quarterly dividends to holders of its common stock. On July 17, 2012, the Board of Directors declared a cash dividend of \$0.27 per common share payable to shareholders of record on August 1, 2012. This dividend is payable on August 15, 2012. The Company estimates its total capital expenditures for the remainder of 2012 will be between \$45.0 million and \$55.0 million. Capital expenditures for the remainder of 2012 are expected to include costs associated with expansion of the Company's distribution infrastructure and the construction of the new manufacturing facility in the Millen, Georgia area.

The Company maintains a \$25.0 million unsecured line of credit with Wells Fargo Bank, N.A. As of June 30, 2012, there was no outstanding debt under the credit agreement. The Company anticipates that cash on hand, cash provided by operating activities and funds available under its line of credit will be sufficient to meet planned operating expenses, tax obligations, capital expenditures and other cash needs for the next 12 months. Based on these assumptions, the Company believes that its fixed costs could be met even with a moderate decrease in demand for the Company's products.

## **Off-Balance Sheet Arrangements**

The Company had no off-balance sheet arrangements as of June 30, 2012.

## **Forward-Looking Information**

The statements in this Form 10-Q that are not historical statements, including statements regarding our future financial and operating performance and liquidity and capital resources, are forward-looking statements within the meaning of the federal securities laws. All forward-looking statements are based on management's current expectations and estimates, which involve risks and uncertainties that could cause actual results to differ materially from those expressed in the forward-looking statements. Among these factors are:

changes in overall economic conditions,

changes in the cost of raw materials and natural gas used in manufacturing our products,

changes in demand and prices charged for our products,

changes in the demand for, or price of, oil and natural gas,

risks of increased competition,

technological, manufacturing and product development risks,

loss of key customers,

changes in foreign and domestic government regulations, including environmental restrictions on operations and regulation of hydraulic fracturing,

changes in foreign and domestic political and legislative risks,

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the risks of war and international and domestic terrorism,

risks associated with foreign operations and foreign currency exchange rates and controls, and

weather-related risks and other risks and uncertainties.

Additional factors that could affect our future results or events are described from time to time in our reports filed with the Securities and Exchange Commission (the "SEC"). See in particular our annual report on Form 10-K for the fiscal year ended December 31, 2011 under the caption "Risk Factors" and similar disclosures in subsequently filed reports with the SEC. We assume no obligation to update forward-looking statements, except as required by law.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The Company's major market risk exposure is to foreign currency fluctuations that could impact its investments in China and Russia. As of June 30, 2012, the Company's net investment that is subject to foreign currency fluctuations totaled \$86.8 million and the Company has recorded a cumulative foreign currency translation loss of \$4.6 million, net of deferred income tax benefit. This cumulative translation loss is included in Accumulated Other Comprehensive Loss. From time to time, the Company may enter into forward foreign exchange contracts to hedge the impact of foreign currency fluctuations. There were no such foreign exchange contracts outstanding at June 30, 2012.

**ITEM 4. CONTROLS AND PROCEDURES**

**(a) Evaluation of Disclosure Controls and Procedures**

Disclosure controls and procedures are designed to ensure that information required to be disclosed in the reports filed or submitted under the Securities Exchange Act of 1934 (the "Exchange Act") is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in the reports filed under the Exchange Act is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

As of June 30, 2012, management carried out an evaluation, under the supervision and with the participation of the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurances of achieving their control objectives. Based upon and as of the date of that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective to ensure that information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms, and to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

**(b) Changes in Internal Control over Financial Reporting**

There were no changes in the Company's internal control over financial reporting during the quarter ended June 30, 2012, that materially affected, or are reasonably likely to materially affect, those controls.

**PART II. OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS**

On February 9, 2012, the Company, Gary A. Kolstad and Ernesto Bautista III, were named as defendants in a purported class-action lawsuit filed in the United States District Court for the Southern District of New York (the "February SDNY Lawsuit"), brought on behalf of shareholders who purchased the Company's Common Stock between October 27, 2011 and January 26, 2012 (the "Relevant Time Period"). The suit alleges violations of the federal securities laws arising from statements concerning the Company's business operations and business prospects that were made



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during the class period and requests unspecified damages and costs. On April 10, 2012, a second purported class-action lawsuit was filed against the same defendants in the United States District Court for the Southern District of New York, brought on behalf of investors who purchased or sold CARBO Ceramics Inc. option contracts during the Relevant Time Period (the April SDNY Lawsuit, and collectively with the February SDNY Lawsuit, the Federal Securities Lawsuit), which alleges substantially similar claims as the February SDNY Lawsuit and requests unspecified damages and costs. In June 2012, the February SDNY Lawsuit and the April SDNY Lawsuit were consolidated, and will now proceed as one lawsuit.

On April 19, 2012, a third purported class-action lawsuit was filed against the same defendants in the United States District Court for the Southern District of Texas, which was also brought on behalf of shareholders who purchased shares during the Relevant Time Period. This lawsuit alleged substantially similar claims as the February SDNY Lawsuit and requested unspecified damages and costs. In June 2012, this lawsuit was dismissed without prejudice.

On March 1, 2012, the Directors of the Company and Mr. Bautista were named as defendants in a purported derivative action lawsuit brought on behalf of the Company by a stockholder in District Court in Harris County, Texas (the March Harris County Lawsuit). The suit alleges various breaches of fiduciary duty and other duties by the defendants that generally are related to the February SDNY Lawsuit, and requests unspecified damages and costs. The parties to this lawsuit have entered into an agreement to stay further proceedings pending the outcome of a motion to dismiss the Federal Securities Lawsuit.

On June 13, 2012, the Directors of the Company and Mr. Bautista were named as defendants in a second purported derivative action lawsuit brought on behalf of the Company by a stockholder in District Court in Harris County, Texas (this lawsuit collectively with the March Harris County Lawsuit, the Harris County Lawsuits). This lawsuit alleges substantially similar claims as the March Harris County Lawsuit as well as a breach of duty against certain defendants in connection with stock sales. This lawsuit also requests unspecified damages and costs. The parties to this lawsuit have entered into an agreement to stay further proceedings pending the outcome of a motion to dismiss the Federal Securities Lawsuit.

While each of the Federal Securities Lawsuit and the Harris County Lawsuits are in their preliminary stages, the Company does not believe they have merit, and plans to vigorously contest and defend against them.

Additionally, from time to time, the Company is the subject of legal proceedings arising in the ordinary course of business. The Company does not believe that any of these proceedings will have a material effect on its business or its results of operations.

The Company cannot predict the ultimate outcome or duration of any lawsuit described in this report.

### **ITEM 1A. RISK FACTORS**

There have been no material changes to the risk factors discussed in the Annual Report on Form 10-K for the year ended December 31, 2011.

### **ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

The following table provides information about the Company's repurchases of Common Stock during the quarter ended June 30, 2012:

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## ISSUER PURCHASES OF EQUITY SECURITIES

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plan	Maximum Number of Shares that May Yet be Purchased Under the Plan(1)
04/01/12 to 04/30/12		\$		122,424
05/01/12 to 05/31/12		\$		122,424
06/01/12 to 06/30/12		\$		122,424

Total

- (1) On August 28, 2008, the Company announced the authorization by its Board of Directors for the repurchase of up to two million shares of its Common Stock.

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable

## ITEM 4. MINE SAFETY DISCLOSURE

Our U.S. manufacturing facilities process mined minerals, and therefore are viewed as mine operations subject to regulation by the federal Mine Safety and Health Administration under the Federal Mine Safety and Health Act of 1977. Information concerning mine safety violations or other regulatory matters required by section 1503(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act and the recently proposed Item 106 of Regulation S-K (17 CFR 229.106) is included in Exhibit 95 to this quarterly report.

## ITEM 5. OTHER INFORMATION

Not applicable

## ITEM 6. EXHIBITS

The following exhibits are filed as part of, or incorporated by reference into, this Quarterly Report on Form 10-Q:

3.1 Restated Certificate of Incorporation

31.1 Rule 13a-14(a)/15d-14(a) Certification by Gary A. Kolstad.

31.2 Rule 13a-14(a)/15d-14(a) Certification by Ernesto Bautista III.

32 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

## Edgar Filing: CARBO CERAMICS INC - Form 10-Q

95 Mine Safety Disclosure

101 The following financial information from the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2012, formatted in XBRL: (i) Consolidated Balance Sheets; (ii) Consolidated Statements of Income; (iii) Consolidated Statements of Comprehensive Income; (iv) Consolidated Statements of Cash Flows; and (v) Notes to the Consolidated Financial Statements.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

CARBO CERAMICS INC.

/s/ Gary A. Kolstad  
Gary A. Kolstad  
President and Chief Executive Officer

/s/ Ernesto Bautista III  
Ernesto Bautista III  
Chief Financial Officer

Date: August 1, 2012

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EXHIBIT INDEX

EXHIBIT	DESCRIPTION
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32	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
95	Mine Safety Disclosure
101	The following financial information from the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2012, formatted in XBRL: (i) Consolidated Balance Sheets; (ii) Consolidated Statements of Income; (iii) Consolidated Statements of Comprehensive Income; (iv) Consolidated Statements of Cash Flows; and (v) Notes to the Consolidated Financial Statements.