

CARPENTER TECHNOLOGY CORP  
Form 10-Q  
April 26, 2018  
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 March 31, 2018

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 1-5828

CARPENTER TECHNOLOGY CORPORATION  
(Exact name of Registrant as specified in its Charter)

Delaware 23-0458500  
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

1735 Market Street, 15th Floor 19103  
Philadelphia, Pennsylvania  
(Address of principal executive offices) (Zip Code)  
610-208-2000  
(Registrant's telephone number, including area code)

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

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

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer:

Accelerated filer:

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

Emerging growth company

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If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The number of shares outstanding of the issuer's common stock as of April 20, 2018 was 46,929,323.

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Table of Contents

CARPENTER TECHNOLOGY CORPORATION  
FORM 10-Q  
INDEX

	Page
<u>PART I FINANCIAL INFORMATION</u>	
<u>Item 1 Financial Statements</u>	
<u>Consolidated Balance Sheets (unaudited) as of March 31, 2018 and June 30, 2017</u>	3
<u>Consolidated Statements of Income (unaudited) for the Three Months and Nine Months Ended March 31, 2018 and 2017</u>	4
<u>Consolidated Statements of Comprehensive Income (unaudited) for the Three Months and Nine Months Ended March 31, 2018 and 2017</u>	5
<u>Consolidated Statements of Cash Flows (unaudited) for the Nine Months Ended March 31, 2018 and 2017</u>	6
<u>Consolidated Statements of Changes in Equity (unaudited) for the Nine Months Ended March 31, 2018 and 2017</u>	7
<u>Notes to the Consolidated Financial Statements (unaudited)</u>	8
<u>Item 2 Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	26
<u>Item 3 Quantitative and Qualitative Disclosures About Market Risk</u>	46
<u>Item 4 Controls and Procedures</u>	47
<u>PART II OTHER INFORMATION</u>	
<u>Item 1 Legal Proceedings</u>	47
<u>Item 1A Risk Factors</u>	47
<u>Item 2 Unregistered Sales of Equity Securities and Use of Proceeds</u>	47
<u>Item 6 Exhibits</u>	48
<u>Signature</u>	49

Table of Contents

## PART I - FINANCIAL INFORMATION

## Item 1. Financial Statements

CARPENTER TECHNOLOGY CORPORATION  
CONSOLIDATED BALANCE SHEETS

(Unaudited)

(\$ in millions, except share data)

	March 31, 2018	June 30, 2017
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$46.8	\$66.3
Accounts receivable, net	349.3	290.4
Inventories	732.6	690.4
Other current assets	62.6	46.5
Total current assets	1,191.3	1,093.6
Property, plant and equipment, net	1,295.6	1,316.8
Goodwill	273.7	263.4
Other intangibles, net	59.9	64.9
Deferred income taxes	5.6	7.6
Other assets	165.8	131.8
Total assets	\$2,991.9	\$2,878.1
<b>LIABILITIES</b>		
Current liabilities:		
Current portion of long-term debt	\$55.0	\$55.0
Accounts payable	217.7	201.1
Accrued liabilities	128.4	139.9
Total current liabilities	401.1	396.0
Long-term debt, net of current portion	546.3	550.0
Accrued pension liabilities	367.0	378.3
Accrued postretirement benefits	124.0	122.6
Deferred income taxes	130.8	184.8
Other liabilities	51.6	47.8
Total liabilities	1,620.8	1,679.5
Contingencies and commitments (see Note 8)		
<b>STOCKHOLDERS' EQUITY</b>		
Common stock — authorized 100,000,000 shares; issued 55,480,760 shares at March 31, 2018 and 55,349,658 shares at June 30, 2017; outstanding 46,928,592 shares at March 31, 2018 and 46,753,180 shares at June 30, 2017	277.4	276.7
Capital in excess of par value	299.8	284.8
Reinvested earnings	1,441.7	1,321.8
Common stock in treasury (8,552,168 shares and 8,596,478 shares at March 31, 2018 and June 30, 2017, respectively), at cost	(339.8 )	(341.6 )
Accumulated other comprehensive loss	(308.0 )	(343.1 )
Total stockholders' equity	1,371.1	1,198.6
Total liabilities and stockholders' equity	\$2,991.9	\$2,878.1

See accompanying notes to consolidated financial statements.



Table of ContentsCARPENTER TECHNOLOGY CORPORATION  
CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(\$ in millions, except per share data)

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2018	2017	2018	2017
Net sales	\$572.2	\$473.6	\$1,539.7	\$1,289.9
Cost of sales	476.2	390.5	1,272.4	1,098.3
Gross profit	96.0	83.1	267.3	191.6
Selling, general and administrative expenses	50.8	47.3	139.6	139.0
Operating income	45.2	35.8	127.7	52.6
Interest expense	(7.5 )	(7.7 )	(22.0 )	(22.5 )
Other income, net	—	1.0	0.9	2.0
Income before income taxes	37.7	29.1	106.6	32.1
Income tax expense (benefit)	7.5	8.4	(39.1 )	10.6
Net income	\$30.2	\$20.7	\$145.7	\$21.5
EARNINGS PER COMMON SHARE:				
Basic	\$0.63	\$0.44	\$3.06	\$0.45
Diluted	\$0.63	\$0.44	\$3.04	\$0.45
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING:				
Basic	47.2	47.0	47.2	47.0
Diluted	47.7	47.1	47.5	47.1
Cash dividends per common share	\$0.18	\$0.18	\$0.54	\$0.54

See accompanying notes to consolidated financial statements.

Table of Contents

CARPENTER TECHNOLOGY CORPORATION  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
(Unaudited)  
(\$ in millions)

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2018	2017	2018	2017
Net income	\$30.2	\$20.7	\$145.7	\$21.5
Other comprehensive income, net of tax				
Pension and postretirement benefits, net of tax of \$(1.2), \$(3.5), \$(3.2) and \$(17.4), respectively	2.1	5.7	6.7	28.8
Net gain on derivative instruments, net of tax of \$(2.7), \$(4.3), \$(13.2) and \$(13.2), respectively	1.3	7.2	24.4	21.8
Foreign currency translation	3.7	2.6	4.0	(2.1 )
Other comprehensive income	7.1	15.5	35.1	48.5
Comprehensive income	\$37.3	\$36.2	\$180.8	\$70.0

See accompanying notes to consolidated financial statements.



Table of ContentsCARPENTER TECHNOLOGY CORPORATION  
CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(\$ in millions)

	Nine Months Ended March 31,	
	2018	2017
<b>OPERATING ACTIVITIES</b>		
Net income	\$145.7	\$21.5
Adjustments to reconcile net income to net cash provided from operating activities:		
Depreciation and amortization	87.2	88.8
Deferred income taxes	(68.9 )	37.4
Net pension expense	10.6	39.7
Share-based compensation expense	12.8	10.0
Net loss on disposals of property and equipment and assets held for sale	2.0	2.2
Changes in working capital and other:		
Accounts receivable	(54.4 )	(15.0 )
Inventories	(41.1 )	(89.0 )
Other current assets	(15.6 )	3.6
Accounts payable	16.9	40.6
Accrued liabilities	5.5	4.9
Pension plan contributions	(5.7 )	(100.0)
Other postretirement plan contributions	(2.5 )	(2.4 )
Other, net	(1.8 )	(6.0 )
Net cash provided from operating activities	90.7	36.3
<b>INVESTING ACTIVITIES</b>		
Purchases of property, equipment and software	(80.9 )	(63.1 )
Proceeds from disposals of property and equipment and assets held for sale	2.0	—
Acquisition of businesses	(13.3 )	(35.3 )
Proceeds from note receivable from the sale of equity method investment	6.3	6.3
Net cash used for investing activities	(85.9 )	(92.1 )
<b>FINANCING ACTIVITIES</b>		
Credit agreement borrowings	—	122.1
Credit agreement repayments	—	(122.1)
Net change in short-term credit agreement borrowings	—	14.2
Payments of debt issue costs	—	(1.4 )
Dividends paid	(25.8 )	(25.6 )
Tax benefits on share-based compensation	—	0.4
Proceeds from stock options exercised	4.5	2.2
Withholding tax payments on share-based compensation awards	(0.9 )	(0.8 )
Net cash used for financing activities	(22.2 )	(11.0 )
Effect of exchange rate changes on cash and cash equivalents	(2.1 )	1.4
<b>DECREASE IN CASH AND CASH EQUIVALENTS</b>	<b>(19.5 )</b>	<b>(65.4 )</b>
Cash and cash equivalents at beginning of period	66.3	82.0
Cash and cash equivalents at end of period	\$46.8	\$16.6
<b>SUPPLEMENTAL CASH FLOW INFORMATION:</b>		
Non-cash investing activities:		
Acquisition of property, equipment and software	\$12.9	\$5.8

See accompanying notes to consolidated financial statements.

6

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Table of Contents

CARPENTER TECHNOLOGY CORPORATION  
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY  
FOR THE NINE MONTHS ENDED MARCH 31, 2018 AND 2017

(Unaudited)

(\$ in millions, except per share data)

	Common Stock Par Value of \$5	Capital in Excess of Par Value	Reinvested Earnings	Common Stock in Treasury	Accumulated Other Comprehensive (Loss) Income	Total Equity
Balances at June 30, 2017	\$276.7	\$ 284.8	\$ 1,321.8	\$(341.6)	\$ (343.1 )	\$ 1,198.6
Net income			145.7			145.7
Pension and postretirement benefits gain, net of tax					6.7	6.7
Net gain on derivative instruments, net of tax					24.4	24.4
Foreign currency translation					4.0	4.0
Cash Dividends:						0
Common @ \$0.54 per share			(25.8 )			(25.8 )
Share-based compensation plans		11.2		1.8		13.0
Stock options exercised	0.7	3.8				4.5
Balances at March 31, 2018	\$277.4	\$ 299.8	\$ 1,441.7	\$(339.8)	\$ (308.0 )	\$ 1,371.1

	Common Stock Par Value of \$5	Capital in Excess of Par Value	Reinvested Earnings	Common Stock in Treasury	Accumulated Other Comprehensive (Loss) Income	Total Equity
Balances at June 30, 2016	\$276.3	\$ 273.5	\$ 1,308.9	\$(343.9)	\$ (409.9 )	\$ 1,104.9
Net income			21.5			21.5
Pension and postretirement benefits gain, net of tax					28.8	28.8
Net gain on derivative instruments, net of tax					21.8	21.8
Foreign currency translation					(2.1 )	(2.1 )
Cash Dividends:						0
Common @ \$0.54 per share			(25.6 )			(25.6 )
Share-based compensation plans		7.9		1.8		9.7
Stock options exercised	0.4	1.8				2.2
Tax windfall on share-based compensation		0.4				0.4
Balances at March 31, 2017	\$276.7	\$ 283.6	\$ 1,304.8	\$(342.1)	\$ (361.4 )	\$ 1,161.6

See accompanying notes to consolidated financial statements.

Table of Contents

CARPENTER TECHNOLOGY CORPORATION  
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

1. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments, consisting of normal and recurring adjustments, considered necessary for a fair statement of the results are reflected in the interim periods presented. The June 30, 2017 consolidated balance sheet data was derived from audited financial statements, but does not include all of the disclosures required by accounting principles generally accepted in the United States of America. These unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and footnotes thereto included in Carpenter's Annual Report on Form 10-K for the fiscal year ended June 30, 2017 (the "2017 Form 10-K"). Operating results for the three and nine months ended March 31, 2018 are not necessarily indicative of the operating results for any future period.

As used throughout this report, unless the context requires otherwise, the terms "Carpenter", the "Company", "Registrant", "Issuer", "we" and "our" refer to Carpenter Technology Corporation.

During the nine months ended March 31, 2018, the Company changed the presentation of borrowings and repayments made under its revolving credit facility in the consolidated statements of cash flows. Prior year amounts have been reclassified to conform to the nine months ended March 31, 2018 presentation.

2. Acquisitions and Divestiture

On February 21, 2018, the Company acquired all of the outstanding membership interests of MB CalRAM LLC ("CalRAM"), for a cash purchase price of \$13.3 million. The acquisition provides the Company with immediate entry into the rapidly expanding part production segment of the additive manufacturing value chain. The preliminary purchase price allocation was as follows: \$0.2 million of working capital, \$2.8 million of property and equipment and \$10.3 million of goodwill. The preliminary purchase price allocation was estimated due to the timing of the acquisition. The final purchase price allocation may change in future reporting periods upon finalization of the valuation analysis, which the Company expects to occur in the fourth quarter of fiscal year 2018.

On February 28, 2017, the Company acquired substantially all the assets of Puris LLC ("Puris"), for a cash purchase price of \$35.3 million. The acquisition provides the Company with immediate entry into the rapidly growing titanium powder market, an expanded presence in additive manufacturing and strengthens the Company's capabilities as a solutions provider for customers across its end-use markets. The purchase price allocation was as follows: \$1.7 million of working capital, \$6.5 million of property and equipment, \$8.5 million of identifiable intangible assets and \$18.6 million of goodwill.

In the fourth quarter of fiscal year 2017, the Company divested its Specialty Steel Supply ("SSS") business. The divestiture was completed in two separate transactions for total cash proceeds of \$12.0 million. The operations of the SSS business were historically included in the Performance Engineered Products ("PEP") segment. The Company has no continuing involvement with the operations of SSS after the divestiture.

### 3. Earnings per Common Share

The Company calculates basic and diluted earnings per share using the two class method. Under the two class method, earnings are allocated to common stock and participating securities (non-vested restricted shares and units that receive non-forfeitable dividends) according to their participation rights in dividends and undistributed earnings. The earnings available to each class of stock are divided by the weighted average number of outstanding shares for the period in each class. Diluted earnings per share assumes the issuance of common stock for all potentially dilutive share equivalents outstanding.

Table of ContentsCARPENTER TECHNOLOGY CORPORATION  
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

The calculations of basic and diluted earnings per common share for the three and nine months ended March 31, 2018 and 2017 were as follows:

	Three Months Ended		Nine Months Ended	
	March 31,		March 31,	
(in millions, except per share data)	2018	2017	2018	2017
Net income	\$30.2	\$20.7	\$145.7	\$21.5
Less: earnings and dividends allocated to participating securities	(0.3 )	(0.1 )	(1.3 )	(0.2 )
Earnings available for common stockholders used in calculation of basic earnings per common share	\$29.9	\$20.6	\$144.4	\$21.3
Weighted average number of common shares outstanding, basic	47.2	47.0	47.2	47.0
Basic earnings per common share	\$0.63	\$0.44	\$3.06	\$0.45
Net income	\$30.2	\$20.7	\$145.7	\$21.5
Less: earnings and dividends allocated to participating securities	(0.3 )	(0.1 )	(1.3 )	(0.2 )
Earnings available for common stockholders used in calculation of diluted earnings per common share	\$29.9	\$20.6	\$144.4	\$21.3
Weighted average number of common shares outstanding, basic	47.2	47.0	47.2	47.0
Effect of shares issuable under share-based compensation plans	0.5	0.1	0.3	0.1
Weighted average number of common shares outstanding, diluted	47.7	47.1	47.5	47.1
Diluted earnings per common share	\$0.63	\$0.44	\$3.04	\$0.45

The following awards issued under share-based compensation plans were excluded from the above calculations of diluted earnings per share because their effects were anti-dilutive:

	Three Months Ended		Nine Months Ended	
(in millions)	March 31, 2018	March 31, 2017	March 31, 2018	March 31, 2017
Stock options	0.7	2.0	0.9	1.9

Table of ContentsCARPENTER TECHNOLOGY CORPORATION  
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

## 4. Inventories

Inventories consisted of the following components as of March 31, 2018 and June 30, 2017:

(\$ in millions)	March 31, June 30,	
	2018	2017
Raw materials and supplies	\$ 168.7	\$ 152.8
Work in process	379.4	365.6
Finished and purchased products	184.5	172.0
Total inventory	\$ 732.6	\$ 690.4

Inventories are valued at the lower of cost or market. Cost for inventories is principally determined using the last-in, first-out (“LIFO”) inventory costing method. The Company also uses the first-in, first-out (“FIFO”) and average cost methods. As of March 31, 2018 and June 30, 2017, \$136.3 million and \$107.3 million of inventory, respectively, was accounted for using a method other than the LIFO inventory costing method.

## 5. Accrued Liabilities

Accrued liabilities consisted of the following as of March 31, 2018 and June 30, 2017:

(\$ in millions)	March 31, June 30,	
	2018	2017
Accrued compensation and benefits	\$ 65.7	\$ 59.1
Accrued postretirement benefits	15.5	15.5
Deferred revenue	12.1	9.8
Accrued interest expense	5.6	11.2
Derivative financial instruments	1.2	13.1
Other	28.3	31.2
Total accrued liabilities	\$ 128.4	\$ 139.9

Table of Contents

CARPENTER TECHNOLOGY CORPORATION  
 NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS  
 (Unaudited)

## 6. Pension and Other Postretirement Benefits

The components of the net periodic benefit cost related to the Company's pension and other postretirement benefits for the three and nine months ended March 31, 2018 and 2017 were as follows:

Three months ended March 31,	Pension Plans		Other Postretirement Plans	
	2018	2017	2018	2017
(\$ in millions)				
Service cost	\$2.4	\$2.2	\$0.7	\$0.9
Interest cost	13.0	12.4	2.4	2.3
Expected return on plan assets	(16.5)	(16.6)	(1.7 )	(1.7 )
Amortization of net loss	3.4	9.5	0.7	0.8
Amortization of prior service cost (benefit)	0.5	0.5	(1.3 )	(1.6 )
Net periodic benefit costs	\$2.8	\$8.0	\$0.8	\$0.7
			Other Postretirement Plans	
Nine months ended March 31,	Pension Plans		Other Postretirement Plans	
	2018	2017	2018	2017
(\$ in millions)				
Service cost	\$7.1	\$18.1	\$2.0	\$2.8
Interest cost	39.1	37.8	7.2	6.9
Expected return on plan assets	(49.5)	(48.4 )	(5.2 )	(5.1 )
Amortization of net loss	10.2	28.3	2.2	2.4
Amortization of prior service cost (benefit)	1.5	&		