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MASCO CORP /DE/
Form 10-Q
April 25, 2019

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2019

Commission file number: 1-5794

Masco Corporation

(Exact name of Registrant as Specified in its Charter)

Delaware

38-1794485

(State of Incorporation) (I.R.S. Employer Identification No.)

17450 College Parkway, Livonia, Michigan 48152

(Address of Principal Executive Offices) (Zip Code)

(313) 274-7400

(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.

x Yes o No

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Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files).

Yes No

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

Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company
(Do not check if a smaller reporting company) Emerging growth company

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Shares Outstanding at March 31, 2019
Common stock, par value \$1.00 per share	293,548,874

MASCO CORPORATION

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MASCO CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)

March 31, 2019 and December 31, 2018
(In Millions, Except Share Data)

	March 31, 2019	December 31, 2018
ASSETS		
Current Assets:		
Cash and cash investments	\$316	\$559
Receivables	1,321	1,153
Prepaid expenses and other	110	108
Inventories:		
Finished goods	592	520
Raw material	319	325
Work in process	100	101
	1,011	946
Total current assets	2,758	2,766
Property and equipment, net	1,222	1,223
Operating lease right-of-use assets	225	—
Goodwill	889	898
Other intangible assets, net	392	406
Other assets	116	100
Total assets	\$5,602	\$5,393
LIABILITIES		
Current Liabilities:		
Accounts payable	\$954	\$926
Notes payable	295	8
Accrued liabilities	680	750
Total current liabilities	1,929	1,684
Long-term debt	2,771	2,971
Other liabilities	860	669
Total liabilities	5,560	5,324
Commitments and contingencies (Note O)		
EQUITY		
Masco Corporation's shareholders' equity:		
Common shares, par value \$1 per share		
Authorized shares: 1,400,000,000;	291	294
Issued and outstanding: 2019 – 291,500,000; 2018 – 293,900,000		
Preferred shares authorized: 1,000,000;		
Issued and outstanding: 2019 and 2018 – None	—	—
Paid-in capital	—	—
Retained deficit	(314)	(278)
Accumulated other comprehensive loss	(123)	(127)
Total Masco Corporation's shareholders' deficit	(146)	(111)

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Noncontrolling interest	188	180
Total equity	42	69
Total liabilities and equity	\$5,602	\$5,393

See notes to condensed consolidated financial statements.

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MASCO CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

For the Three Months Ended March 31, 2019 and 2018
(In Millions, Except Per Common Share Data)

	Three Months Ended March 31,			
	2019		2018	
Net sales	\$	1,908	\$	1,920
Cost of sales		1,309		1,301
Gross profit		599		619
Selling, general and administrative expenses		372		375
Impairment charges for goodwill and other intangible assets		16		—
Operating profit		211		244
Other income (expense), net:				
Interest expense	(39)	(41)
Other, net	(4)	(3)
	(43)	(44)
Income before income taxes		168		200
Income tax expense		41		39
Net income		127		161
Less: Net income attributable to noncontrolling interest		11		12
Net income attributable to Masco Corporation	\$	116	\$	149
Income per common share attributable to Masco Corporation:				
Basic:				
Net income	\$.39	\$.48
Diluted:				
Net income	\$.39	\$.47

See notes to condensed consolidated financial statements.

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MASCO CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (Unaudited)

For the Three Months Ended March 31, 2019 and 2018
(In Millions)

	Three Months Ended March 31,	
	2019	2018
Net income	\$127	\$161
Less: Net income attributable to noncontrolling interest	11	12
Net income attributable to Masco Corporation	\$116	\$149
Other comprehensive income (loss), net of tax (Note K):		
Cumulative translation adjustment	\$(3)	\$42
Pension and other post-retirement benefits	4	5
Other comprehensive income, net of tax	1	47
Less: Other comprehensive (loss) income attributable to noncontrolling interest	(3)	7
Other comprehensive income attributable to Masco Corporation	\$4	\$40
Total comprehensive income	\$128	\$208
Less: Total comprehensive income attributable to noncontrolling interest	8	19
Total comprehensive income attributable to Masco Corporation	\$120	\$189

See notes to condensed consolidated financial statements.

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MASCO CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

For the Three Months Ended March 31, 2019 and 2018
(In Millions)

	Three Months Ended March 31,	
	2019	2018
CASH FLOWS FROM (FOR) OPERATING ACTIVITIES:		
Cash provided by operations	\$183	\$210
Increase in receivables	(181)	(216)
Increase in inventories	(65)	(87)
(Decrease) increase in accounts payable and accrued liabilities, net	(68)	38
Net cash for operating activities	(131)	(55)
CASH FLOWS FROM (FOR) FINANCING ACTIVITIES:		
Purchase of Company common stock	(116)	(150)
Proceeds from revolving credit borrowings, net	87	—
Cash dividends paid	(35)	(33)
Proceeds from the exercise of stock options	9	—
Employee withholding taxes paid on stock-based compensation	(14)	(32)
Payment of debt	(1)	—
Credit Agreement and other financing costs	(2)	—
Net cash for financing activities	(72)	(215)
CASH FLOWS FROM (FOR) INVESTING ACTIVITIES:		
Capital expenditures	(38)	(40)
Acquisition of business, net of cash acquired	—	(548)
Proceeds from disposition of:		
Short-term bank deposits	—	13
Property and equipment	5	1
Other, net	(5)	—
Net cash for investing activities	(38)	(574)
Effect of exchange rate changes on cash and cash investments	(2)	20
CASH AND CASH INVESTMENTS:		
Decrease for the period	(243)	(824)
At January 1	559	1,194
At March 31	\$316	\$370

See notes to condensed consolidated financial statements.

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MASCO CORPORATION
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (Unaudited)

For the Three Months Ended March 31, 2019 and 2018
(In Millions, Except Per Common Share Data)

	Total	Common Shares (\$1 par value)	Paid-In Capital	Retained (Deficit) Earnings	Accumulated Other Comprehensive (Loss) Income	Noncontrolling Interest
Balance, January 1, 2018	\$183	\$ 310	\$ —	\$(298)	\$ (65)	\$ 236
Reclassification of disproportionate tax effects (Refer to Note K)	—			59	(59)	
Total comprehensive income	208			149	40	19
Shares issued	(13)	2	(7)	(8)		
Shares retired:						
Repurchased	(150)	(4)		(146)		
Surrendered (non-cash)	(19)			(19)		
Cash dividends declared	(33)			(33)		
Stock-based compensation	7		7			
Balance, March 31, 2018	\$183	\$ 308	\$ —	\$(296)	\$ (84)	\$ 255
Balance, January 1, 2019	\$69	\$ 294	\$ —	\$(278)	\$ (127)	\$ 180
Total comprehensive income	128			116	4	8
Shares issued	5	1	4			
Shares retired:						
Repurchased	(122)	(3)	(11)	(108)		
Surrendered (non-cash)	(10)	(1)		(9)		
Cash dividends declared	(35)			(35)		
Stock-based compensation	7		7			
Balance, March 31, 2019	\$42	\$ 291	\$ —	\$(314)	\$ (123)	\$ 188

See notes to condensed consolidated financial statements.

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MASCO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

A. ACCOUNTING POLICIES

In our opinion, the accompanying unaudited condensed consolidated financial statements contain all adjustments, of a normal recurring nature, necessary to fairly state our financial position at March 31, 2019, and our results of operations, comprehensive income (loss), cash flows and changes in shareholders' equity for the three-month periods ended March 31, 2019 and 2018. The condensed consolidated balance sheet at December 31, 2018 was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America.

Leases. We determine if an arrangement is a lease at inception. Operating leases are included in operating lease right-of-use assets ("ROU assets"), accrued liabilities and other liabilities on our condensed consolidated balance sheet. Finance lease ROU assets are included in property and equipment, net, notes payable, and long-term debt on our condensed consolidated balance sheet.

ROU assets represent our right to use an underlying asset for the duration of the lease term while lease liabilities represent our obligation to make lease payments in exchange for the right to use an underlying asset. ROU assets and lease liabilities are measured based on the present value of fixed lease payments over the lease term at the commencement date. The ROU asset also includes any lease payments made prior to the commencement date and initial direct costs incurred, and is reduced by any lease incentives received. We review our ROU assets as events occur or circumstances change that would indicate the carrying amount of the ROU assets are not recoverable and exceed their fair values. If the carrying amount of the ROU asset is not recoverable from its undiscounted cash flows, then we would recognize an impairment loss for the difference between the carrying amount and the current fair value.

As most of our leases do not provide an implicit rate, we generally use our incremental borrowing rate on the commencement date of the lease as the discount rate in determining the present value of future lease payments. We determine the incremental borrowing rate for each lease by using the current yields of our uncollateralized, publicly traded debts with maturity periods similar to the respective lease term, adjusted to a collateralized basis based on third-party data. Our lease terms may include options to extend or terminate the lease when there are relevant economic incentives present that make it reasonably certain that we will exercise that option. We account for any non-lease components separately from lease components.

For operating leases, lease expense for future fixed lease payments is recognized on a straight-line basis over the lease term. For finance leases, lease expense for future fixed lease payments is recognized using the effective interest rate method over the lease term. Variable lease payments are recognized as lease expense in the period incurred. Leases with an initial term of 12 months or less are not recorded on the balance sheet; we recognize lease expense for these leases on a straight-line basis over the lease term.

Recently Adopted Accounting Pronouncements. In February 2016, the Financial Accounting Standards Board ("FASB") issued a new standard for leases, ASC 842, which changes the accounting model for identifying and accounting for leases. We adopted ASC 842 on January 1, 2019 using the optional transition method, which allows for initial application of the new standard beginning at the adoption date. We elected the package of practical expedients that allows us to forgo reassessing a) whether any existing contracts are or contain leases, b) the lease classification for any existing leases, and c) whether initial direct costs for any existing leases are capitalized. We also elected the practical expedient to use hindsight with respect to lease renewals, terminations, and purchase options when determining the lease term and in assessing impairment of the assets related to leases existing at the time of adoption. As a result of the standard, we recorded \$236 million of operating lease ROU assets, \$45 million of short-term operating lease liabilities, and \$214 million of long-term operating lease liabilities on the date of adoption. Our

accounting for finance leases remained unchanged. The standard did not impact our condensed consolidated statements of operations or statements of cash flows.

In August 2017, the FASB issued ASU 2017-12, "Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities," which improves and simplifies accounting rules around hedge accounting and better portrays the economic results of an entity's risk management activities in its financial statements. We adopted ASU 2017-12 on January 1, 2019. The adoption of the standard did not impact our financial position or results of operations.

MASCO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (Continued)

A. ACCOUNTING POLICIES (Concluded)

In June 2018, the FASB issued ASU 2018-07, "Compensation-Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting," which modifies the accounting for share-based payment awards issued to nonemployees to largely align it with the accounting for share-based payment awards issued to employees.

We adopted ASU 2018-07 on January 1, 2019. The adoption of the standard did not impact our financial position or results of operations.

Recently Issued Accounting Pronouncements. In June 2016, the FASB issued ASU 2016-13, "Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments," which modifies the methodology for recognizing loss impairments on certain types of financial instruments, including receivables. The new methodology requires an entity to estimate the credit losses expected over the life of an exposure. Additionally, ASU 2016-13 amends the current available-for-sale security other-than-temporary impairment model for debt securities. ASU 2016-13 is effective for us for annual periods beginning January 1, 2020. We are currently evaluating the impact the adoption of this new standard will have on our financial position and results of operations.

In August 2018, the FASB issued ASU 2018-15, "Intangibles-Goodwill and Other-Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract," which allows for the capitalization of certain implementation costs incurred in a hosting arrangement that is a service contract. ASU 2018-15 allows for either retrospective adoption or prospective adoption to all implementation costs incurred after the date of adoption. ASU 2018-15 is effective for us for annual periods beginning January 1, 2020. We are currently evaluating the impact the adoption of this new standard will have on our financial position and results of operations.

B. ACQUISITIONS

On March 9, 2018, we acquired substantially all of the net assets of The L.D. Kichler Co. ("Kichler"), a leader in decorative residential and light commercial lighting products, ceiling fans and LED lighting systems. This business expands our product offerings to our customers. The results of this acquisition for the period from the acquisition date are included in the condensed consolidated financial statements and are reported in the Decorative Architectural Products segment. The purchase price, net of \$2 million cash acquired, consisted of \$549 million paid with cash on hand. Since the acquisition, we revised the allocation of the purchase price to identifiable assets and liabilities based on analysis of information as of the acquisition date that was made available in the year after acquisition. The initial and final allocations of the fair value of the acquisition of Kichler is summarized in the following table, in millions.

	Initial	Final
Receivables	\$101	\$100
Inventories	173	166
Other current assets	5	5
Property and equipment	33	33
Goodwill	46	64
Other intangible assets	243	240
Accounts payable	(24)	(24)
Accrued liabilities	(25)	(30)

Other liabilities	(4)	(5)
Total	\$548	\$549

The goodwill acquired, which is generally tax deductible, is related primarily to the operational and financial synergies we expect to derive from combining Kichler's operations into our business, as well as the assembled workforce. The other intangible assets acquired consist of \$59 million of indefinite-lived intangible assets, which is related to trademarks, and \$181 million of definite-lived intangible assets. The definite-lived intangible assets consist of \$145 million related to customer relationships, which is being amortized on a straight-line basis over 20 years, and \$36 million of other definite-lived intangible assets, which is being amortized over a weighted average amortization period of 3 years.

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MASCO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (Continued)

C. REVENUE

Our revenues are derived primarily from sales to customers in North America and Internationally, principally Europe. Net sales from these geographic markets, by segment, were as follows, in millions: