

MUELLER INDUSTRIES INC
Form 10-Q
July 27, 2012
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

FORM 10-Q

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

For the quarterly period ended June 30,
2012

Commission file number 1-6770

MUELLER INDUSTRIES, INC.
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction
of incorporation or organization)

25-0790410
(I.R.S. Employer
Identification No.)

8285 Tournament Drive, Suite 150
Memphis, Tennessee
(Address of principal executive offices)

38125
(Zip Code)

(901) 753-3200
(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

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
Non-accelerated filer

Accelerated filer
Smaller reporting company

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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 of the Registrant's common stock outstanding as of July 25, 2012, was 38,258,700.

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MUELLER INDUSTRIES, INC.

FORM 10-Q

For the Quarterly Period Ended June 30, 2012

As used in this report, the terms “Company,” “Mueller,” and “Registrant” mean Mueller Industries, Inc. and its consolidated subsidiaries taken as a whole, unless the context indicates otherwise.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

MUELLER INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

(In thousands, except per share data)	For the Quarter Ended		For the Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
Net sales	\$ 594,099	\$ 652,923	\$ 1,171,767	\$ 1,340,604
Cost of goods sold	522,851	573,877	1,016,026	1,163,751
Depreciation and amortization	7,919	9,166	15,448	18,865
Selling, general, and administrative expense	33,487	33,330	65,089	68,699
Insurance settlement	—	—	(1,500)	—
Litigation settlement	—	—	—	(10,500)
Operating income	29,842	36,550	76,704	99,789
Interest expense	(2,721)	(2,834)	(5,358)	(6,182)
Other income, net	490	264	744	1,323
Income before income taxes	27,611	33,980	72,090	94,930
Income tax expense	(9,071)	(11,249)	(20,733)	(31,657)
Consolidated net income	18,540	22,731	51,357	63,273
Net income attributable to noncontrolling interest	(623)	(400)	(841)	(355)
Net income attributable to Mueller Industries, Inc.	\$ 17,917	\$ 22,331	\$ 50,516	\$ 62,918
Weighted average shares for basic earnings per share	38,029	37,737	38,021	37,730
Effect of dilutive stock-based awards	436	356	440	309
Adjusted weighted average shares for diluted earnings per share	38,465	38,093	38,461	38,039
Basic earnings per share	\$ 0.47	\$ 0.59	\$ 1.33	\$ 1.67
Diluted earnings per share	\$ 0.47	\$ 0.59	\$ 1.31	\$ 1.65
Dividends per share	\$ 0.10	\$ 0.10	\$ 0.20	\$ 0.20

See accompanying notes to condensed consolidated financial statements.

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MUELLER INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

(In thousands)	For the Quarter Ended		For the Six Months Ended	
	June 30, 2012	July 2, 2011	June 30, 2012	July 2, 2011
Consolidated net income	\$ 18,540	\$ 22,731	\$ 51,357	\$ 63,273
Other comprehensive (loss) income, net of tax:				
Foreign currency translation	(4,545)	1,256	2,199	8,248
Net change with respect to derivative instruments and hedging activities, net	(658) ¹	544 ²	309 ³	(233) ⁴
Other, net	880	395	1,140	432
Total other comprehensive (loss) income	(4,323)	2,195	3,648	8,447
Consolidated comprehensive income	14,217	24,926	55,005	71,720
Comprehensive income attributable to noncontrolling interest	(451)	(755)	(1,030)	(970)
Comprehensive income attributable to Mueller Industries, Inc.	\$ 13,766	\$ 24,171	\$ 53,975	\$ 70,750

See accompanying notes to condensed consolidated financial statements.

1 Net of tax of \$415

2 Net of tax of \$(268)

3 Net of tax of \$(166)

4 Net of tax of \$141

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MUELLER INDUSTRIES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

(In thousands, except share data)	June 30, 2012	December 31, 2011
Assets		
Current assets:		
Cash and cash equivalents	\$ 373,680	\$ 514,162
Accounts receivable, less allowance for doubtful accounts of \$1,413 in 2012 and \$1,564 in 2011	299,264	250,027
Inventories	229,338	219,193
Current deferred income taxes	21,463	21,104
Other current assets	20,305	22,213
Total current assets	944,050	1,026,699
Property, plant, and equipment, net	212,035	203,744
Goodwill	102,250	102,250
Other assets	14,105	14,911
Total Assets	\$ 1,272,440	\$ 1,347,604
Liabilities		
Current liabilities:		
Current portion of debt	\$ 25,715	\$ 41,265
Accounts payable	89,914	65,545
Accrued wages and other employee costs	32,886	39,319
Other current liabilities	91,871	67,115
Total current liabilities	240,386	213,244
Long-term debt, less current portion	7,800	156,476
Pension liabilities	31,821	32,839
Postretirement benefits other than pensions	21,341	21,405
Environmental reserves	22,600	22,892
Deferred income taxes	13,079	14,856
Other noncurrent liabilities	966	1,130
Total liabilities	337,993	462,842
Equity		
Mueller Industries, Inc. stockholders' equity:		
Preferred stock - \$1.00 par value; shares authorized 5,000,000; none outstanding	—	—
Common stock - \$.01 par value; shares authorized 100,000,000; issued 40,091,502; outstanding 38,266,097 in 2012 and 38,236,568 in 2011	401	401
Additional paid-in capital	269,105	266,936
Retained earnings	725,244	682,380
Accumulated other comprehensive loss	(45,950)	(49,409)

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Treasury common stock, at cost	(44,457)	(44,620)
Total Mueller Industries, Inc. stockholders' equity	904,343	855,688
Noncontrolling interest	30,104	29,074
Total equity	934,447	884,762
Commitments and contingencies	—	—
Total Liabilities and Equity	\$ 1,272,440	\$ 1,347,604

See accompanying notes to condensed consolidated financial statements.

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MUELLER INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(In thousands)	For the Six Months Ended	
	June 30, 2012	July 2, 2011
Cash flows from operating activities		
Consolidated net income	\$ 51,357	\$ 63,273
Reconciliation of consolidated net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	15,843	18,999
Stock-based compensation expense	2,061	1,712
Insurance settlement	(1,500)	—
Insurance proceeds – noncapital related	9,000	—
Loss (gain) on disposal of properties	106	(275)
Deferred income taxes	(2,930)	(2,549)
Income tax benefit from exercise of stock options	(83)	(90)
Changes in assets and liabilities, net of business acquired:		
Receivables	(55,826)	(55,010)
Inventories	(9,055)	(78,966)
Other assets	(1,371)	(4,398)
Current liabilities	9,121	17,199
Other liabilities	285	768
Other, net	270	433
Net cash provided by (used in) operating activities	17,278	(38,904)
Cash flows from investing activities		
Capital expenditures	(23,433)	(8,743)
Acquisition of business	—	(6,882)
Insurance proceeds for property and equipment	32,500	—
Net withdrawals from (deposits into) restricted cash balances	4,368	(3,877)
Proceeds from sales of properties	175	151
Net cash provided by (used in) investing activities	13,610	(19,351)
Cash flows from financing activities		
Dividends paid to stockholders of Mueller Industries, Inc.	(7,605)	(7,546)
Debt issuance cost	—	(1,942)
(Repayment) issuance of debt by joint venture, net	(15,842)	16,498
Net proceeds from the exercise of stock options	187	592
Repayments of long-term debt	(148,676)	(250)
Income tax benefit from exercise of stock options	83	90

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Net cash (used in) provided by financing activities	(171,853)	7,442
Effect of exchange rate changes on cash	483	1,713
Decrease in cash and cash equivalents	(140,482)	(49,100)
Cash and cash equivalents at the beginning of the period	514,162	394,139
Cash and cash equivalents at the end of the period	\$ 373,680	\$ 345,039

See accompanying notes to condensed consolidated financial statements.

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MUELLER INDUSTRIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

General

Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted. Results of operations for the interim periods presented are not necessarily indicative of results which may be expected for any other interim period or for the year as a whole. This Quarterly Report on Form 10-Q should be read in conjunction with the Company's Annual Report on Form 10-K, including the annual financial statements incorporated therein.

The accompanying unaudited interim financial statements include all normal recurring adjustments which are, in the opinion of management, necessary to a fair statement of the results for the interim periods presented.

Note 1 – Earnings per Common Share

Basic per share amounts have been computed based on the average number of common shares outstanding. Diluted per share amounts reflect the increase in average common shares outstanding that would result from the assumed exercise of outstanding stock options and vesting of restricted stock awards, computed using the treasury stock method.

Note 2 – Commitments and Contingencies

The Company is involved in certain litigation as a result of claims that arose in the ordinary course of business, which management believes will not have a material adverse effect on the Company's financial position, results of operations, or cash flows. The Company may also realize the benefit of certain legal claims and litigation in the future; these gain contingencies are not recognized in the Condensed Consolidated Financial Statements.

Extruded Metals Class Action

A purported class action was filed in Michigan Circuit Court by Gaylord L. Miller, and all others similarly situated, against a subsidiary of the Company, Extruded Metals, Inc., in March 2012 under nuisance, negligence, and gross negligence theories. It is brought on behalf of all persons in the City of Belding, Michigan, whose property rights have allegedly been interfered with by fallout and/or dust and/or noxious odors, allegedly attributable to Extruded Metals' operations. Plaintiffs allege that they have suffered interference with the use and enjoyment of their properties. They seek compensatory and exemplary damages and injunctive relief. The Company intends to vigorously defend this matter. At this time, the Company is unable to determine the impact, if any, that this matter will have on its financial position, results of operations, or cash flows.

Supplier Litigation

On May 6, 2011, the Company and two of its subsidiaries, Mueller Streamline Co. (Mueller Streamline) and B&K Industries, Inc. (B&K)(Plaintiffs), filed a civil lawsuit in federal district court in Los Angeles, California against a former supplier, Xiamen Lota International Co., Ltd (Xiamen Lota), its U.S. sales representative (Lota USA), and

certain other persons (Defendants). The lawsuit alleges, among other things, that the Defendants gave Peter D. Berkman, a former executive of the Company and B&K, an undisclosed interest in Lota USA, and made payments and promises of payments to him, in return for Peter Berkman maintaining the Company as a customer, increasing purchasing levels, and acquiescing to non-competitive and excessive pricing for Xiamen Lota products. The lawsuit alleges violations of federal statutes 18 U.S.C. Sections 1962(c) and (d) (RICO claims) and California state law unfair competition. The lawsuit seeks compensatory, treble and punitive damages, and other appropriate relief including an award of reasonable attorneys' fees and costs of suit. All of the foreign Defendants have been served under the Hague Convention and Xiamen Lota has withdrawn its motion contesting service of process (filed July 1, 2011). On January 4, 2012, the foreign Defendants filed a motion to dismiss all of the claims in the Company's Complaint for failure to state claims, and also joined in Lota USA's pending motion to dismiss (filed July 1, 2011). On December 16, 2011, the Court granted Lota USA's motion to disqualify the Company's counsel and the Company has retained new counsel to represent it going forward in the lawsuit. The motions to dismiss were heard on April 9, 2012, and the Court sustained Plaintiffs' unfair competition claim, and dismissed without prejudice and with leave to amend, their RICO claims. The Plaintiffs filed an amended complaint on April 30, 2012. Defendants moved to dismiss on May 17, 2012. The parties await the Court's ruling. A mediation will be held August 14 and 15, 2012. The Court set a trial date for this civil matter to commence on June 18, 2013.

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U.K. Actions Relating To The European Commission's 2004 Copper Tubes Decision And 2006 Copper Fittings Decision

Mueller Industries, Inc., WTC Holding Company, DENO Holding Company, Inc., Mueller Europe, Limited, and DENO Acquisition EURL (the Mueller entities) received a letter from counsel for IMI plc and IMI Kynoch Limited (IMI) concerning contribution proceedings by IMI against the Mueller entities regarding copper tubes. In the Competition Appeal Tribunal (the CAT) in the United Kingdom, IMI has been served with claims by 21 claimants, all companies within the Travis Perkins Group (TP and the TP Claimants). The TP Claimants are seeking follow-on damages arising out of the Copper Tubes Cartel, as described in the European Commission's September 3, 2004 decision. The claims thus arise from the findings of the European Commission as set forth in that decision.

Mueller Industries, Inc., Mueller Europe, Limited, and WTC Holding Company also received a letter from counsel for IMI concerning contribution proceedings by IMI against those three Mueller entities regarding copper fittings. In the High Court, IMI has been served with claims by 21 TP Claimants. The TP Claimants are seeking follow-on damages arising out of the Copper Fittings Cartel, as described in the European Commission's September 20, 2006 decision. The claims similarly arise from the findings of the European Commission as set forth in that decision.

The letters confirm that IMI has commenced (but not yet formally served) legal proceedings against the Mueller entities, and in those proceedings will be claiming a contribution for any follow-on losses.

While the TP Claimants have provided their preliminary calculations of aggregate claimed damages for the Copper Tubes Cartel and the Copper Fittings Cartel, Mueller is unable at this time to estimate its potential liability, if any, for the contribution claims.

As to the claims arising from the Copper Tubes Decision, brought in the CAT, the CAT has now granted approval for the case to be transferred to the High Court.

Lead Refinery Site

On July 12, 2012, the U. S. Environmental Protection Agency (EPA) proposed a remedy that consists of removal of contaminated soils which is subject to further review and consideration, as well as public comment, before it becomes final. There is no assurance that the remedy as proposed by EPA will be adopted, or that the EPA's current estimate of cost of approximately \$29 million is reliable. Lead Refinery is currently unable to predict whether it might incur liability related to this site, or to estimate the extent of such liability or whether it would be material. EPA has also notified two other potentially responsible parties (PRPs) at the site; the allocation of costs, if any among the PRPs is unknown.

Other

Guarantees, in the form of letters of credit, are issued by the Company generally to assure the payment of insurance deductibles and certain retiree health benefits. The terms of the Company's guarantees are generally one year but are renewable annually as required. These letters are primarily backed by the Company's line of credit facility. The maximum payments that the Company could be required to make under its guarantees at June 30, 2012, was \$13.0 million.

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Note 3 – Insurance Claims

Fulton, Mississippi, Copper Tube Facility

In July 2009, there was an explosion at the Company’s copper tube facility in Fulton, Mississippi resulting in damage to certain production equipment. In the first quarter of 2012, the Company settled the business interruption portion of this claim and recognized a \$1.5 million gain.

Wynne, Arkansas, Copper Tube Facility

In September 2011, a portion of the Company’s Wynne, Arkansas, manufacturing operation was damaged by fire. Certain inventories, production equipment, and building structures were extensively damaged. The total value of the loss, including business interruption, cannot be determined at this time, but is expected to be covered by property and business interruption insurance subject to customary deductibles. Any gain resulting from insurance proceeds for property damage in excess of the net book value of the related property will be recognized in income upon settlement of the claim. In addition, the Company has deferred recognition of direct, identifiable costs associated with this matter. These costs will also be recognized upon settlement of the insurance claim. As of June 30, 2012, the Company has received advances totaling \$50 million from the insurance company for this claim, of which \$40 million was received during the first half of 2012. These advances, net of the book value of damaged inventories, equipment, and buildings and direct cleanup and other out of pocket costs totaled \$31.7 million, classified as other current liabilities on the Condensed Consolidated Balance Sheet at June 30, 2012.

Note 4 – Inventories

(In thousands)	June 30, 2012	December 31, 2011
Raw materials and supplies	\$ 51,522	\$ 42,281
Work-in-process	28,639	38,420
Finished goods	154,521	143,648
Valuation reserves	(5,344)	(5,156)
Inventories	\$ 229,338	\$ 219,193

The Company has partially liquidated inventories valued using the last-in, first-out (LIFO) method during the first half of 2012. The Company expects to replenish these inventories by the end of 2012 and, as such, has not recognized the effects of liquidating LIFO layers. In the event these inventories are not replenished, due to lack of availability or operational reasons, the Company would recognize a reduction to cost of goods sold of approximately \$18.2 million from the liquidation of LIFO layers based on quarter-end quantities.

During 2011, inventory quantities valued using the LIFO method declined which resulted in liquidation of LIFO inventory layers. This liquidation resulted from intercompany sales; therefore, the gain from the LIFO liquidation of approximately \$8.0 million was deferred. During the first quarter of 2012, the Company sold this inventory to third parties and recognized the gain. This recognition resulted in a reduction of approximately \$8.0 million to cost of sales, or \$0.13 per diluted share after tax.

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Note 5 – Debt

(In thousands)	June 30, 2012	December 31, 2011
6% Subordinated Debentures, due 2014	\$ —	\$ 148,176
2001 Series IRB's with interest at 1.39%, due through 2021	8,750	9,250
Mueller-Xingrong line of credit with interest at 6.00%, due 2012	24,715	40,265
Other	50	50
	33,515	197,741
Less current portion of debt	(25,715)	(41,265)
Long-term debt	\$ 7,800	\$ 156,476

On May 24, 2012, the Company issued a Notice of Full Redemption of its outstanding 6% Subordinated Debentures, due 2014 (the “Debentures,” and the transaction whereby the Debentures were redeemed, the “Redemption”). The Debentures were redeemed on June 25, 2012 at par value totaling approximately \$148.2 million principal and accrued interest of approximately \$1.3 million.

Note 6 – Industry Segments

The Company's reportable segments are Plumbing & Refrigeration and Original Equipment Manufacturers (OEM). For disclosure purposes, as permitted under Accounting Standards Codification (ASC) 280, Segment Reporting, certain operating segments are aggregated into reportable segments. The Plumbing & Refrigeration segment is composed of Standard Products (SPD), European Operations, and Mexican Operations. The OEM segment is composed of Industrial Products (IPD), Engineered Products (EPD), and Jiangsu Mueller-Xingrong Copper Industries Limited (Mueller-Xingrong). These segments are classified primarily by the markets for their products. Performance of segments is generally evaluated by their operating income. Intersegment transactions are generally conducted on an arms-length basis.

SPD manufactures copper tube and fittings, plastic fittings, plastic pipe, and line sets. These products are manufactured in the U.S. Outside the U.S., the Company's European Operations manufacture copper tube, which is sold in Europe and the Middle East. SPD also imports and resells brass and plastic plumbing valves, malleable iron fittings, faucets, and plumbing specialty products. Mexican Operations consist of pipe nipple manufacturing and import distribution businesses including product lines of malleable iron fittings and other plumbing specialties. The European Operations consist of copper tube manufacturing and the import distribution of fittings, valves, and plumbing specialties primarily in the U.K. and Ireland. The Plumbing & Refrigeration segment's products are sold primarily to plumbing, refrigeration, and air-conditioning wholesalers, hardware wholesalers and co-ops, and building product retailers.

IPD manufactures brass rod, impact extrusions, and forgings which are used in a wide variety of end products including plumbing brass, automotive components, valves, and fittings. EPD manufactures and fabricates valves and assemblies primarily for the refrigeration, air-conditioning, and gas appliance markets and specialty copper, copper-alloy, and aluminum tubing. Mueller-Xingrong manufactures engineered copper tube primarily for air-conditioning applications. These products are sold primarily to OEM customers.

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Summarized segment information is as follows:

(In thousands)	For the Quarter Ended June 30, 2012			
	Plumbing & Refrigeration Segment	OEM Segment	Corporate and Eliminations	Total
Net sales	\$ 331,688	\$ 268,551	\$ (6,140)	\$ 594,099
Cost of goods sold	285,182	243,646	(5,977)	522,851
Depreciation and amortization	4,151	3,412	356	7,919
Selling, general, and administrative expense	19,750	6,436	7,301	33,487
Operating income	22,605	15,057	(7,820)	29,842
Interest expense				(2,721)
Other income, net				490
Income before income taxes				\$ 27,611

(In thousands)	For the Quarter Ended July 2, 2011			
	Plumbing & Refrigeration Segment	OEM Segment	Corporate and Eliminations	Total
Net sales	\$ 347,069	\$ 314,086	\$ (8,232)	\$ 652,923
Cost of goods sold	296,033	285,944	(8,100)	573,877
Depreciation and amortization	5,349	3,479	338	9,166
Selling, general, and administrative expense	20,897	5,847	6,586	33,330
Operating income	24,790	18,816	(7,056)	36,550
Interest expense				(2,834)
Other income, net				264
Income before income taxes				\$ 33,980

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(In thousands)	For the Six Months Ended June 30, 2012			
	Plumbing & Refrigeration Segment	OEM Segment	Corporate and Eliminations	Total
Net sales	\$ 647,042	\$ 539,527	\$ (14,802)	\$ 1,171,767
Cost of goods sold	550,653	479,846	(14,473)	1,016,026
Depreciation and amortization	8,296	6		