

MATTHEWS INTERNATIONAL CORP
Form 10-Q
February 03, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

Form 10-Q

x Quarterly report under Section 13 or 15(d) of the Securities Exchange Act of 1934

For The Quarterly Period Ended December 31, 2010

Commission File No. 0-9115

MATTHEWS INTERNATIONAL CORPORATION
(Exact Name of registrant as specified in its charter)

PENNSYLVANIA
(State or other jurisdiction of
Incorporation or organization)

25-0644320
(I.R.S. Employer
Identification No.)

TWO NORTHSORE CENTER,
PITTSBURGH, PA
(Address of principal executive offices)

15212-5851
(Zip Code)

Registrant's telephone number, including area
code

(412) 442-8200

NOT APPLICABLE

(Former name, former address and former fiscal year, if changed since last report)

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 x No o

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes x No o

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

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Large accelerated filer Accelerated filer Non-accelerated filer 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 January 31, 2011, shares of common stock outstanding were:

Class A Common Stock 29,587,092 shares

PART I - FINANCIAL INFORMATION
MATTHEWS INTERNATIONAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)
(Dollar amounts in thousands, except per share data)

	December 31, 2010	September 30, 2010
ASSETS		
Current assets:		
Cash and cash equivalents	\$53,724	\$59,715
Short-term investments	1,394	1,395
Accounts receivable, net	139,410	151,038
Inventories	116,497	107,926
Deferred income taxes	1,662	1,666
Other current assets	14,121	13,915
Total current assets	326,808	335,655
Investments	15,674	13,642
Property, plant and equipment: Cost	309,531	308,630
Less accumulated depreciation	(181,969)	(178,880)
	127,562	129,750
Deferred income taxes	32,450	30,555
Other assets	20,904	21,101
Goodwill	427,994	405,180
Other intangible assets, net	59,327	57,942
Total assets	\$1,010,719	\$993,825
LIABILITIES		
Current liabilities:		
Long-term debt, current maturities	\$11,561	\$12,073
Accounts payable	38,351	36,308
Accrued compensation	27,787	39,062
Accrued income taxes	14,939	12,984
Other current liabilities	45,716	47,686
Total current liabilities	138,354	148,113
Long-term debt	236,626	225,256
Accrued pension	51,227	50,276
Postretirement benefits	23,612	23,307
Deferred income taxes	15,609	15,950
Environmental reserve	5,835	5,961
Other liabilities	37,589	31,234
Total liabilities	508,852	500,097
SHAREHOLDERS' EQUITY		

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Shareholders' equity-Matthews:			
Common stock	36,334	36,334	
Additional paid-in capital	43,941	48,294	
Retained earnings	632,768	621,923	
Accumulated other comprehensive loss	(38,315)	(37,136)	
Treasury stock, at cost	(203,916)	(207,470)	
Total shareholders' equity-Matthews		470,812	461,945
Noncontrolling interests		31,055	31,783
Total shareholders' equity		501,867	493,728
Total liabilities and shareholders' equity		\$1,010,719	\$993,825

The accompanying notes are an integral part of these consolidated financial statements.

MATTHEWS INTERNATIONAL CORPORATION AND SUBSIDIARIES
 CONSOLIDATED STATEMENTS OF INCOME (Unaudited)
 (Dollar amounts in thousands, except per share data)

	Three Months Ended December 31,	
	2010	2009
Sales	\$207,344	\$192,973
Cost of sales	(127,599)	(119,583)
Gross profit	79,745	73,390
Selling and administrative expenses	(57,779)	(51,214)
Operating profit	21,966	22,176
Investment income	1,151	1,195
Interest expense	(1,752)	(1,939)
Other deductions, net	(269)	(98)
Income before income taxes	21,096	21,334
Income taxes	(7,573)	(7,678)
Net income	13,523	13,656
Net income attributable to noncontrolling interests	(309)	(660)
Net income attributable to Matthews shareholders	\$13,214	\$12,996
Earnings per share attributable to Matthews shareholders:		
Basic	\$.46	\$.43
Diluted	\$.45	\$.43

The accompanying notes are an integral part of these consolidated financial statements.

MATTHEWS INTERNATIONAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
for the three months ended December 31, 2010 and 2009 (Unaudited)
(Dollar amounts in thousands, except per share data)

	Shareholders' Equity - Matthews						
	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Non- controlling interests	Total
Balance, September 30, 2010	\$ 36,334	\$ 48,294	\$ 621,923	\$ (37,136)	\$ (207,470)	\$ 31,783	\$ 493,728
Net income	-	-	13,214	-	-	309	13,523
Minimum pension liability	-	-	-	803	-	-	803
Translation adjustment	-	-	-	(2,459)	-	(451)	(2,910)
Fair value of derivatives	-	-	-	477	-	-	477
Total comprehensive income							11,893
Stock-based compensation	-	1,757	-	-	-	-	1,757
Purchase of 81,543 shares of treasury stock	-	-	-	-	(2,743)	-	(2,743)
Issuance of 208,076 shares of treasury stock	-	(6,110)	-	-	6,297	-	187
Dividends, \$.08 per share	-	-	(2,369)	-	-	-	(2,369)
Distributions to noncontrolling interests						(586)	(586)
Balance, December 31, 2010	\$ 36,334	\$ 43,941	\$ 632,768	\$ (38,315)	\$ (203,916)	\$ 31,055	\$ 501,867

Shareholders' Equity - Matthews
Accumulated
Other

Additional

Non-

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	Common Stock	Paid-in Capital	Retained Earnings	Comprehensive Income (Loss)	Treasury Stock	controlling interests	Total
Balance, September 30, 2009	\$36,334	\$47,436	\$559,786	\$ (29,884)	\$(179,454)	\$4,676	\$438,894
Net income	-	-	12,996	-	-	660	13,656
Minimum pension liability	-	-	-	789	-	-	789
Translation adjustment	-	-	-	(3,967)	-	(10)	(3,977)
Fair value of derivatives	-	-	-	399	-	-	399
Total comprehensive income							10,867
Stock-based compensation	-	1,609	-	-	-	-	1,609
Purchase of 146,636 shares of treasury stock	-	-	-	-	(5,143)	-	(5,143)
Issuance of 206,959 shares of treasury stock	-	(5,440)	-	-	6,169	-	729
Dividends, \$.07 per share	-	-	(2,127)	-	-	-	(2,127)
Balance, December 31, 2009	\$36,334	\$43,605	\$570,655	\$ (32,663)	\$(178,428)	\$5,326	\$444,829

The accompanying notes are an integral part of these consolidated financial statements.

MATTHEWS INTERNATIONAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)
(Dollar amounts in thousands, except per share data)

	Three Months Ended December 31,	
	2010	2009
Cash flows from operating activities:		
Net income	\$ 13,523	\$ 13,656
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	6,761	6,331
Gain on investments	(400)	(351)
(Gain) loss on sale of assets	(118)	46
Stock-based compensation expense	1,757	1,609
Change in deferred taxes	(867)	(1,083)
Changes in working capital items	(2,740)	6,824
Decrease (increase) in other assets	197	(2,421)
Decrease in other liabilities	(856)	(3,467)
Increase in pension and postretirement benefits	2,573	2,501
 Net cash provided by operating activities	 19,830	 23,645
Cash flows from investing activities:		
Capital expenditures	(3,748)	(4,176)
Proceeds from sale of assets	155	58
Acquisitions, net of cash acquired	(26,659)	(9,511)
Purchases of investments	(1,606)	(1,612)
 Net cash used in investing activities	 (31,858)	 (15,241)
Cash flows from financing activities:		
Proceeds from long-term debt	23,862	14,210
Payments on long-term debt	(12,048)	(12,822)
Proceeds from the sale of treasury stock	153	672
Purchases of treasury stock	(2,743)	(5,143)
Excess tax benefit of share-based compensation arrangements	34	56
Dividends	(2,369)	(2,127)
Distributions to noncontrolling interests	(586)	-
 Net cash provided by (used in) financing activities	 6,303	 (5,154)
 Effect of exchange rate changes on cash	 (266)	 (1,154)
 Net change in cash and cash equivalents	 \$(5,991)	 \$ 2,096

The accompanying notes are an integral part of these consolidated financial statements.

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MATTHEWS INTERNATIONAL CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

December 31, 2010

(Dollar amounts in thousands, except per share data)

Note 1. Nature of Operations

Matthews International Corporation ("Matthews" or the "Company"), founded in 1850 and incorporated in Pennsylvania in 1902, is a designer, manufacturer and marketer principally of memorialization products and brand solutions. Memorialization products consist primarily of bronze and granite memorials, other memorialization products, caskets and cremation equipment for the cemetery and funeral home industries. Brand solutions include graphics imaging products and services, marking products and merchandising solutions. The Company's products and operations are comprised of six business segments: Bronze, Casket, Cremation, Graphics Imaging, Marking Products and Merchandising Solutions. The Bronze segment is a leading manufacturer of cast bronze and granite memorials, other memorialization products, cast and etched architectural products and is a leading builder of mausoleums in the United States. The Casket segment is a leading casket manufacturer and distributor in North America and produces a wide variety of wood and metal caskets. The Cremation segment is a leading designer and manufacturer of cremation equipment and cremation caskets primarily in North America. The Graphics Imaging segment provides brand management, printing plates, gravure cylinders, pre-press services and imaging services for the primary packaging and corrugated industries. The Marking Products segment designs, manufactures and distributes a wide range of marking and coding equipment and consumables, and industrial automation products for identifying, tracking and conveying various consumer and industrial products, components and packaging containers. The Merchandising Solutions segment designs and manufactures merchandising displays and systems and provides creative merchandising and marketing solutions services.

The Company has manufacturing and marketing facilities in the United States, Mexico, Canada, Europe, Australia and Asia.

Note 2. Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information for commercial and industrial companies and the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. The year-end condensed balance sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for fair presentation have been included. Operating results for the three months ended December 31, 2010 are not necessarily indicative of the results that may be expected for the fiscal year ending September 30, 2011. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended September 30, 2010. The consolidated financial statements include all domestic and foreign subsidiaries in which the Company maintains an ownership interest and has operating control. All intercompany accounts and transactions have been eliminated.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and

disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued
(Dollar amounts in thousands, except per share data)

Note 3. Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. It establishes a three level fair value hierarchy to prioritize the inputs used in valuations, as defined below:

Level 1: Observable inputs that reflect unadjusted quoted prices for identical assets or liabilities in active markets.

Level 2: Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3: Unobservable inputs for the asset or liability.

As of December 31, 2010 and September 30, 2010, the fair values of the Company's assets and liabilities measured on a recurring basis are categorized as follows:

	December 31, 2010				September 30, 2010			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Assets:								
Short-term investments	\$1,394	-	-	\$1,394	\$1,395	-	-	\$1,395
Trading securities	13,776	-	-	13,776	11,770	-	-	11,770
Total assets at fair value	\$15,170	-	-	\$15,170	\$13,165	-	-	\$13,165
Liabilities:								
Derivatives (1)	-	\$3,662	-	\$3,662	-	\$4,445	-	\$4,445
Total liabilities at fair value	-	\$3,662	-	\$3,662	-	\$4,445	-	\$4,445

(1) Interest rate swaps are valued based on observable market swap rates.

Note 4. Inventories

Inventories consisted of the following:

	December 31, 2010	September 30, 2010
Materials and finished goods	\$ 98,025	\$ 93,737
Labor and overhead in process	18,472	14,189
	\$ 116,497	\$ 107,926

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued
(Dollar amounts in thousands, except per share data)

Note 5. Debt

On December 21, 2010, the Company entered into a new domestic Revolving Credit Facility with a syndicate of financial institutions. The maximum amount of borrowings available under the new facility is \$300,000 and borrowings under the facility bear interest at LIBOR plus a factor ranging from 1.00% to 1.50% based on the Company's leverage ratio. The facility's maturity is December 2015. The new facility replaced the Company's \$225,000 Revolving Credit Facility. The leverage ratio is defined as net indebtedness divided by EBITDA (earnings before interest, taxes, depreciation and amortization). The Company is required to pay an annual commitment fee ranging from .20% to .30% (based on the Company's leverage ratio) of the unused portion of the facility.

The Revolving Credit Facility requires the Company to maintain certain leverage and interest coverage ratios. A portion of the facility (not to exceed \$25,000) is available for the issuance of commercial and standby letters of credit. Outstanding borrowings on the Revolving Credit Facilities were \$203,000 and \$187,000 as of December 31, 2010 and September 30, 2010, respectively. The weighted-average interest rate on outstanding borrowings on these facilities at December 31, 2010 and 2009 was 2.89% and 2.92%, respectively.

The Company has entered into the following interest rate swaps:

Date	Amount	Interest Rate Spread		
		Fixed Interest Rate	at December 31, 2010	Maturity Date
September 2007	\$25,000	4.77%	1.25%	September 2012
May 2008	30,000	3.72%	1.25%	September 2012
October 2008	20,000	3.46%	1.25%	October 2011

The interest rate swaps have been designated as cash flow hedges of the future variable interest payments under the Revolving Credit Facility which are considered probable of occurring. Based on the Company's assessment, all of the critical terms of each of the hedges matched the underlying terms of the hedged debt and related forecasted interest payments, and as such, these hedges were considered highly effective.

The fair value of the interest rate swaps reflected an unrealized loss of \$3,662 (\$2,234 after tax) at December 31, 2010 that is included in shareholders' equity as part of accumulated other comprehensive income. Assuming market rates remain constant with the rates at December 31, 2010, approximately \$1,437 of the \$2,234 loss included in accumulated other comprehensive income is expected to be recognized in earnings as an adjustment to interest expense over the next twelve months.

At December 31, 2010 and September 30, 2010, the interest rate swap contracts were reflected as a liability on the balance sheets. The following derivatives are designated as hedging instruments:

Liability Derivatives		
Balance Sheet Location:	December 31, 2010	September 30, 2010
Current liabilities:		
Other current liabilities	\$ 2,355	\$ 2,623

Long-term liabilities				
Other liabilities		1,307		1,822
Total derivatives	\$	3,662	\$	4,445

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued
(Dollar amounts in thousands, except per share data)

Note 5. Debt (continued)

The income recognized on derivatives was as follows:

Derivatives in Cash Flow Hedging Relationships	Location of Gain or (Loss) Recognized in Income on Derivative	Amount of Gain or (Loss) Recognized in Income on Derivatives Three Months Ended December 31, 2010	Amount of Gain or (Loss) Recognized in Income on Derivatives Three Months Ended December 31, 2009
Interest rate swaps	Interest expense	\$ (757)	\$ (947)

The Company recognized the following gains or losses in accumulated other comprehensive loss ("OCL"):

Derivatives in Cash Flow Hedging Relationships	Amount of Gain or (Loss) Recognized in OCL on Derivatives December 31, 2010	Amount of Gain or (Loss) Recognized in OCL on Derivatives December 31, 2009	Location of Gain or (Loss) Reclassified from Accumulated OCL into Income (Effective Portion*)	Amount of Gain or (Loss) Reclassified from Accumulated OCL into Income (Effective Portion*) December 31, 2010	Amount of Gain or (Loss) Reclassified from Accumulated OCL into Income (Effective Portion*) December 31, 2009
Interest rate swaps	\$ 15	\$ (179)	Interest expense	\$ (462)	\$ (578)

*There is no ineffective portion or amount excluded from effectiveness testing.

The Company, through certain of its German subsidiaries, has a credit facility with a European bank. The maximum amount of borrowings available under this facility was 25.0 million Euros (\$33,428). Outstanding borrowings under the credit facility totaled 12.0 million Euros (\$16,045) and 12.0 million Euros (\$16,361) at December 31, 2010 and September 30, 2010, respectively. The weighted-average interest rate on outstanding borrowings under this facility at December 31, 2010 and 2009 was 2.00% and 1.66%, respectively.

The Company, through its German subsidiary, Saueressig GmbH & Co. KG ("Saueressig"), has several loans with various European banks. Outstanding borrowings under these loans totaled 7.6 million Euros (\$10,125) and 7.9 million Euros (\$10,816) at December 31, 2010 and September 30, 2010, respectively. The weighted-average interest rate on outstanding borrowings of Saueressig at December 31, 2010 and 2009 was 6.28% and 5.92%, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued
(Dollar amounts in thousands, except per share data)

Note 5. Debt (continued)

The Company, through its wholly-owned subsidiary, Matthews International S.p.A., has several loans with various Italian banks. Outstanding borrowings on these loans totaled 10.6 million Euros (\$14,127) and 10.8 million Euros (\$14,680) at December 31, 2010 and September 30, 2010, respectively. Matthews International S.p.A. also has three lines of credit totaling 8.4 million Euros (\$11,192) with the same Italian banks. Outstanding borrowings on these lines were 2.6 million Euros (\$3,440) and 2.1 million Euros (\$2,834) at December 31, 2010 and September 30, 2010, respectively. The weighted-average interest rate on outstanding Matthews International S.p.A. borrowings at December 31, 2010 and 2009 was 3.48% and 3.70%, respectively.

As of December 31, 2010 the fair value of the Company's long-term debt, including current maturities, approximated the carrying value included in the Condensed Consolidated Balance Sheet. At September 30, 2010, the fair value of the Company's long-term debt, including current maturities, was approximately \$225,052.

Note 6. Share-Based Payments

The Company maintains an equity incentive plan (the "2007 Equity Incentive Plan") that provides for the grants of stock options, restricted shares, stock-based performance units and certain other types of stock-based awards. Under the 2007 Equity Incentive Plan, which has a ten-year term, the maximum number of shares available for grants or awards is an aggregate of 2,200,000. The Company also maintains a stock incentive plan (the "1992 Incentive Stock Plan") that previously provided for grants of stock options, restricted shares and certain other types of stock-based awards. There will be no further grants under the 1992 Incentive Stock Plan. At December 31, 2010, there were 1,137,344 shares reserved for future issuance under the 2007 Equity Incentive Plan. Both plans are administered by the Compensation Committee of the Board of Directors.

The option price for each stock option granted under either plan may not be less than the fair market value of the Company's common stock on the date of grant. Outstanding stock options are generally exercisable in one-third increments upon the attainment of 10%, 33% and 60% appreciation in the market value of the Company's Class A Common Stock. In addition, options generally vest in one-third increments after three, four and five years, respectively, from the grant date (but, in any event, not until the attainment of the market value thresholds). The options expire on the earlier of ten years from the date of grant, upon employment termination, or within specified time limits following voluntary employment termination (with the consent of the Company), retirement or death. The Company generally settles employee stock option exercises with treasury shares. With respect to outstanding restricted share grants, generally one-half of the shares vest on the third anniversary of the grant. For shares granted prior to fiscal 2011, the remaining one-half of the shares vest in one-third increments upon attainment of 10%, 25% and 40% appreciation in the market value of the Company's Class A Common Stock. For shares granted in fiscal 2011, the remaining one-half of the shares vest in one-third increments upon attainment of 5%, 15% and 25% appreciation in the market value of the Company's Class A Common Stock. Additionally, beginning in fiscal 2009, restricted shares cannot vest until the first anniversary of the grant date. Unvested restricted shares generally expire on the earlier of five years from the date of grant, upon employment termination, or within specified time limits following voluntary employment termination (with the consent of the Company), retirement or death. The Company issues restricted shares from treasury shares.

For the three-month periods ended December 31, 2010 and 2009, total stock-based compensation cost totaled \$1,757 and \$1,609, respectively. The associated future income tax benefit recognized was \$685 and \$627 for the three-month

periods ended December 31, 2010 and 2009, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued
(Dollar amounts in thousands, except per share data)

Note 6. Share-Based Payments (continued)

For the three-month periods ended December 31, 2010 and 2009, the amount of cash received from the exercise of stock options was \$153 and \$672, respectively. In connection with these exercises, the tax benefits realized by the Company for the three-month periods ended December 31, 2010 and 2009 were \$60 and \$262, respectively.

The transactions for restricted stock for the three months ended December 31, 2010 were as follows:

	Shares	Weighted- average grant-date fair value
Non-vested at September 30, 2010	437,442	\$36.06
Granted	198,710	30.78
Vested	(56,440)	43.79
Expired or forfeited	-	-
Non-vested at December 31, 2010	579,712	33.50

As of December 31, 2010, the total unrecognized compensation cost related to unvested restricted stock was \$8,238 and is expected to be recognized over a weighted average period of 1.7 years.

The transactions for shares under options for the quarter ended December 31, 2010 were as follows:

	Shares	Weighted- average exercise price	Weighted- average remaining contractual term	Aggregate intrinsic value
Outstanding, September 30, 2010	953,326	\$36.32		
Granted	-	-		
Exercised	(9,366)	16.36		
Expired or forfeited	(1,099)	27.70		
Outstanding, December 31, 2010	942,861	36.53	4.7	\$-
Exercisable, December 31, 2010	577,281	35.06	4.3	\$-

No shares were earned during the three months ended December 31, 2010. The fair value of shares earned during the three-month period ended December 31, 2009 was \$3,411. The intrinsic value of options (which is the amount by which the stock price exceeded the exercise price of the options on the date of exercise) exercised during the three-month periods ended December 31, 2010 and 2009 was \$161 and \$417, respectively.

The transactions for non-vested options for the quarter ended December 31, 2010 were as follows:

	Shares	Weighted-average grant-date fair value
Non-vested shares		

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Non-vested at September 30, 2010	366,179	\$	13.54
Granted	-		-
Vested	-		-
Expired or forfeited	(599)	12.41
Non-vested at December 31, 2010	365,580		13.54

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued
(Dollar amounts in thousands, except per share data)

Note 6. Share-Based Payments (continued)

As of December 31, 2010, the total unrecognized compensation cost related to non-vested stock options was approximately \$203. This cost is expected to be recognized over a weighted-average period of 0.9 years in accordance with the vesting periods of the options.

The fair value of each restricted stock grant is estimated on the date of grant using a binomial lattice valuation model. The following table indicates the assumptions used in estimating fair value of restricted stock granted during the periods ended December 31, 2010 and 2009.

	Three Months Ended December 31,			
	2010		2009	
Expected volatility	30.0	%	30.0	%
Dividend yield	1.0	%	.8	%
Average risk free interest rate	1.2	%	2.3	%
Weighted-average expected term (years)	2.0		2.2	

The risk free interest rate is based on United States Treasury yields at the date of grant. The dividend yield is based on the most recent dividend payment and average stock price over the 12 months prior to the grant date. Expected volatilities are based on the historical volatility of the Company's stock price. The expected term represents an estimate of the average period of time for restricted shares to vest. The option characteristics for each grant are considered separately for valuation purposes.

Under the Company's Director Fee Plan, directors (except for the Chairman of the Board) who are not also officers of the Company each receive, as an annual retainer fee, either cash or shares of the Company's Class A Common Stock equivalent to \$60. The equivalent amount paid to a non-employee Chairman of the Board is \$130. Where the annual retainer fee is provided in shares, each director may elect to be paid these shares on a current basis or have such shares credited to a deferred stock account as phantom stock, with such shares to be paid to the director subsequent to leaving the Board. The value of deferred shares is recorded in other liabilities. A total of 25,013 shares had been deferred under the Director Fee Plan at December 31, 2010. Additionally, directors who are not also officers of the Company each receive an annual stock-based grant (non-statutory stock options, stock appreciation rights and/or restricted shares) with a value of \$70. A total of 22,300 stock options have been granted under the plan. At December 31, 2010, 17,800 options were outstanding and vested. Additionally, 51,525 shares of restricted stock have been granted under the plan, 23,420 of which were unvested at December 31, 2010. A total of 300,000 shares have been authorized to be issued under the Director Fee Plan.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued
(Dollar amounts in thousands, except per share data)

Note 7. Earnings Per Share Attributable to Matthews Shareholders

	Three Months Ended December 31,	
	2010	2009
Net income attributable to Matthews shareholders	\$ 13,214	\$ 12,996
Weighted-average common shares outstanding	29,027,227	29,974,606
Dilutive securities, primarily stock options	201,365	214,441
Diluted weighted-average common shares outstanding	29,228,592	30,189,047
Basic earnings per share	\$.46	\$.43
Diluted earnings per share	\$.45	\$.43

Options to purchase 613,868 and 1,005,471 shares of common stock were not included in the computation of diluted earnings per share for the three months ended December 31, 2010 and 2009, respectively, because the inclusion of these options would be anti-dilutive.

Note 8. Pension and Other Postretirement Benefit Plans

The Company provides defined benefit pension and other postretirement plans to certain employees. Net periodic pension and other postretirement benefit cost for the plans included the following:

Three months ended December 31	Pension		Other Postretirement	
	2010	2009	2010	2009
Service cost	\$1,237	\$1,078	\$158	\$173
Interest cost	1,867	1,853	313	346
Expected return on plan assets	(1,843)	(1,717)	-	-
Amortization:				
Prior service cost	6	(10)	(119)	(181)
Net actuarial loss	1,338	1,338	102	130
Net benefit cost	\$2,605	\$2,542	\$454	\$468

Benefit payments under the Company's principal retirement plan are made from plan assets, while benefit payments under the postretirement benefit plan are made from the Company's operating funds. Under IRS regulations, the Company is not required to make any significant contributions to its principal retirement plan in fiscal year 2011. During the three months ended December 31, 2010, contributions of \$186 and \$234 were made under the supplemental retirement plan and postretirement plan, respectively. The Company currently anticipates contributing an additional \$578 and \$859 under the supplemental retirement plan and postretirement plan, respectively, for the remainder of fiscal 2011.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued
(Dollar amounts in thousands, except per share data)

Note 9. Income Taxes

Income tax provisions for the Company's interim periods are based on the effective income tax rate expected to be applicable for the full year. The Company's effective tax rate for the three months ended December 31, 2010 was 35.9%, compared to 36.0% for the first quarter of fiscal 2010. The difference between the Company's fiscal 2011 first quarter effective tax rate and the Federal statutory rate of 35.0% primarily reflected the impact of state and foreign income taxes.

The Company had unrecognized tax benefits (excluding penalties and interest) of \$3,479 and \$3,422 on December 31, 2010 and September 30, 2010, respectively, all of which, if recorded, would impact the 2011 annual effective tax rate. It is reasonably possible that \$347 of the unrecognized tax benefits could be recognized in the next 12 months primarily due to tax examinations and the expiration of statutes related to specific tax positions.

The Company classifies interest and penalties on tax uncertainties as a component of the provision for income taxes. The Company included \$101 in interest and penalties in the provision for income taxes for the first quarter of fiscal 2011. Total penalties and interest accrued were \$2,513 and \$2,412 at December 31, 2010 and September 30, 2010, respectively. These accruals may potentially be applicable in the event of an unfavorable outcome of uncertain tax positions.

The Company is currently under examination in several tax jurisdictions and remains subject to examination until the statute of limitations expires for those tax jurisdictions. As of December 31, 2010, the tax years that remain subject to examination by major jurisdiction generally are:

United States –	2007 and forward
Federal	
United States –	2007 and forward
State	
Canada	2006 and forward
Europe	2002 and forward
United Kingdom	2009 and forward
Australia	2006 and forward
Asia	2004 and forward

Note 10. Segment Information

The Company's products and operations consist of two principal businesses that are comprised of three operating segments each, as described under Nature of Operations (Note 1): Memorialization Products (Bronze, Casket, Cremation) and Brand Solutions (Graphics Imaging, Marking Products, Merchandising Solutions). Management evaluates segment performance based on operating profit (before income taxes) and does not allocate non-operating items such as investment income, interest expense, other income (deductions), net and minority interest.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued
(Dollar amounts in thousands, except per share data)

Note 10. Segment Information (continued)

Information about the Company's segments follows:

	Three Months Ended December 31,	
	2010	2009
Sales to external customers:		
Memorialization:		
Bronze	\$50,513	\$49,259
Casket	60,244	50,664
Cremation	9,654	8,500
	120,411	108,423
Brand Solutions:		
Graphics Imaging	60,027	59,806
Marking Products	12,920	11,566
Merchandising Solutions	13,986	13,178
	86,933	84,550
	\$207,344	\$192,973
Operating profit:		
Memorialization:		
Bronze	\$10,127	\$10,360
Casket	5,848	5,808
Cremation	1,052	1,130
	17,027	17,298
Brand Solutions:		
Graphics Imaging	3,718	3,989
Marking Products	1,025	600
Merchandising Solutions	196	289
	4,939	4,878
	\$21,966	\$22,176

Note 11. Acquisitions

In October 2010, the Company acquired Freeman Metal Products, Inc. and its affiliated companies ("Freeman"), a manufacturer and distributor of caskets. The purchase price for the acquisition was \$22,800, plus additional consideration up to \$6,000 contingent on operating performance over the next three years. The transaction is intended to provide synergies in the manufacturing and distribution of caskets and expand the Company's market presence in the Southeast and South Central regions of the United States.

In October 2010, the Company acquired the remaining 25% interest in Rudolf Reproflex GmbH & Co. KG (“Reproflex”). The Company acquired a 75% interest in Reproflex in 2001.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued
(Dollar amounts in thousands, except per share data)

Note 12. Goodwill and Other Intangible Assets

Goodwill related to business combinations is not amortized but is subject to annual review for impairment. In general, when the carrying value of a reporting unit exceeds its implied fair value, an impairment loss must be recognized. For purposes of testing for impairment the Company uses a combination of valuation techniques, including discounted cash flows. Intangible assets are amortized over their estimated useful lives unless such lives are considered to be indefinite. A significant decline in cash flows generated from these assets may result in a write-down of the carrying values of the related assets. The Company performs its annual impairment review in the second fiscal quarter.

A summary of the carrying amount of goodwill attributable to each segment as well as the changes in such amounts are as follows:

	Bronze	Casket	Cremation	Graphics Imaging	Marking Products	Merchandising Solutions	Consolidated
Goodwill	\$88,613	\$140,553	\$16,799	\$149,161	\$10,168	\$ 9,138	\$ 414,432
Accumulated impairment losses	(412)	-	(5,000)	(3,840)	-	-	(9,252)
Balance at September 30, 2010	88,201	140,553	11,799	145,321	10,168	9,138	\$ 405,180
Additions during period	-	20,601	-	4,917	-	-	25,518
Translation and other adjustments	(344)	-	(64)	(2,355)	59	-	(2,704)
Goodwill	88,269	161,154	16,735	151,723	10,227	9,138	437,246
Accumulated impairment losses	(412)	-	(5,000)	(3,840)	-	-	(9,252)
Balance at December 31, 2010	\$87,857	\$161,154	\$11,735	\$147,883	\$10,227	\$ 9,138	\$ 427,994

The addition to Casket goodwill primarily represents the acquisition of Freeman and the addition to Graphics goodwill represents the acquisition of the remaining 25% interest in Reproflex.

The following tables summarize the carrying amounts and related accumulated amortization for intangible assets as of December 31, 2010 and September 30, 2010, respectively.

	Carrying Amount	Accumulated Amortization	Net
December 31, 2010:			