

KENNAMETAL INC
Form 10-Q
November 07, 2013
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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 SEPTEMBER 30, 2013
Commission file number 1-5318
KENNAMETAL INC.
(Exact name of registrant as specified in its charter)

Pennsylvania 25-0900168
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

World Headquarters
1600 Technology Way
P.O. Box 231 15650-0231
Latrobe, Pennsylvania
(Address of principal executive offices) (Zip Code)

Website: www.kennametal.com

Registrant's telephone number, including area code: (724) 539-5000

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. (Check one):

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

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

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

Title of Each Class	Outstanding at October 31, 2013
Capital Stock, par value \$1.25 per share	78,418,844

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FORWARD-LOOKING INFORMATION

This Quarterly Report on Form 10-Q contains “forward-looking” statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements are statements that do not relate strictly to historical or current facts. You can identify forward-looking statements by the fact they use words such as “should,” “anticipate,” “estimate,” “approximate,” “expect,” “may,” “will,” “project,” “intend,” “plan” and other words of similar meaning and expression in connection with any discussion of future operating or financial performance or events. We have also included forward looking statements in this Quarterly Report on Form 10-Q concerning, among other things, our strategy, goals, plans and projections regarding our financial position, liquidity and capital resources, results of operations, market position, and product development. These statements are based on current estimates that involve inherent risks and uncertainties. Should one or more of these risks or uncertainties materialize, or should the assumptions underlying the forward-looking statements prove incorrect, our actual results could vary materially from our current expectations. There are a number of factors that could cause our actual results to differ from those indicated in the forward-looking statements. They include: economic recession; availability and cost of the raw materials we use to manufacture our products; our foreign operations and international markets, such as currency exchange rates, different regulatory environments, trade barriers, exchange controls, and social and political instability; changes in the regulatory environment in which we operate, including environmental, health and safety regulations; our ability to protect and defend our intellectual property; competition; our ability to retain our management and employees; demands on management resources; potential claims relating to our products; integrating acquisitions and achieving the expected savings and synergies; business divestitures; global or regional catastrophic events; energy costs; commodity prices; labor relations; demand for and market acceptance of new and existing products; and implementation of environmental remediation matters. We provide additional information about many of the specific risks we face in the “Risk Factors” Section of our Annual Report on Form 10-K. We can give no assurance that any goal or plan set forth in forward-looking statements can be achieved and readers are cautioned not to place undue reliance on such statements, which speak only as of the date made. We undertake no obligation to release publicly any revisions to forward-looking statements as a result of future events or developments.

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PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

KENNAMETAL INC.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

(in thousands, except per share amounts)	Three Months Ended September 30,	
	2013	2012
Sales	\$619,808	\$629,459
Cost of goods sold	421,571	421,111
Gross profit	198,237	208,348
Operating expense	134,264	138,860
Amortization of intangibles	5,143	5,107
Operating income	58,830	64,381
Interest expense	7,081	5,956
Other expense (income), net	611	(902)
Income before income taxes	51,138	59,327
Provision for income taxes	12,580	12,280
Net income	38,558	47,047
Less: Net income attributable to noncontrolling interests	721	657
Net income attributable to Kennametal	\$37,837	\$46,390
PER SHARE DATA ATTRIBUTABLE TO KENNAMETAL SHAREOWNERS		
Basic earnings per share	\$0.48	\$0.58
Diluted earnings per share	\$0.48	\$0.57
Dividends per share	\$0.18	\$0.16
Basic weighted average shares outstanding	78,439	80,245
Diluted weighted average shares outstanding	79,470	81,405

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

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KENNAMETAL INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

(in thousands)	Three Months Ended	
	2013	2012
Net income	\$38,558	\$47,047
Unrealized loss on derivatives designated and qualified as cash flow hedges, net of income tax benefit of \$0.4 million and \$0.4 million, respectively	(570) (571
Reclassification of unrealized loss on expired derivatives designated and qualified as cash flow hedges, net of income tax benefit of \$0.3 million and \$0.0 million, respectively	409	85
Unrecognized net pension and other postretirement benefit loss, net of income tax benefit of \$0.7 million and \$0.4 million, respectively	(1,966) (1,118
Reclassification of net pension and other postretirement benefit loss, net of income tax benefit of \$0.2 million and \$1.4 million, respectively	484	2,414
Foreign currency translation adjustments, net of income tax expense of (\$1.4) million and (\$1.1) million, respectively	27,910	25,080
Total comprehensive income	64,825	72,937
Comprehensive income attributable to noncontrolling interests	535	1,287
Comprehensive income attributable to Kennametal Shareowners	\$64,290	\$71,650

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

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CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(in thousands, except per share data)	September 30, 2013	June 30, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	\$333,305	\$377,316
Accounts receivable, less allowance for doubtful accounts of \$12,515 and \$11,949	425,436	445,322
Inventories (Note 9)	631,784	578,795
Deferred income taxes	51,351	49,707
Other current assets	52,315	48,333
Total current assets	1,494,191	1,499,473
Property, plant and equipment:		
Land and buildings	391,724	381,215
Machinery and equipment	1,496,634	1,466,942
Less accumulated depreciation	(1,139,789)	(1,106,675)
Property, plant and equipment, net	748,569	741,482
Other assets:		
Investments in affiliated companies	867	671
Goodwill (Note 16)	730,590	721,755
Other intangible assets, less accumulated amortization of \$118,047 and \$111,440 (Note 16)	235,929	222,765
Deferred income taxes	39,268	39,590
Other	80,900	75,303
Total other assets	1,087,554	1,060,084
Total assets	\$3,330,314	\$3,301,039
LIABILITIES		
Current liabilities:		
Current maturities of long-term debt and capital leases (Note 10)	\$143	\$3,738
Notes payable to banks	2,808	40,581
Accounts payable	173,909	190,623
Accrued income taxes	23,561	19,471
Accrued expenses	90,624	88,433
Other current liabilities	133,708	124,747
Total current liabilities	424,753	467,593
Long-term debt and capital leases, less current maturities (Note 10)	703,380	703,626
Deferred income taxes	102,612	102,935
Accrued pension and post retirement benefits	165,974	162,245
Accrued income taxes	25,484	27,530
Other liabilities	34,917	24,817
Total liabilities	1,457,120	1,488,746
Commitments and contingencies		
EQUITY (Note 14)		
Kennametal Shareowners' Equity:		
Preferred stock, no par value; 5,000 shares authorized; none issued	—	—
Capital stock, \$1.25 par value; 120,000 shares authorized; 78,404 and 77,842 shares issued	98,005	97,303

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Additional paid-in capital	383,741	374,300	
Retained earnings	1,422,997	1,399,227	
Accumulated other comprehensive loss	(62,551) (89,004)
Total Kennametal Shareowners' Equity	1,842,192	1,781,826	
Noncontrolling interests	31,002	30,467	
Total equity	1,873,194	1,812,293	
Total liabilities and equity	\$3,330,314	\$3,301,039	

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

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KENNAMETAL INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOW (UNAUDITED)

(in thousands)	Three Months Ended	
	September 30, 2013	2012
OPERATING ACTIVITIES		
Net income	\$38,558	\$47,047
Adjustments for non-cash items:		
Depreciation	22,251	23,884
Amortization	5,143	5,107
Stock-based compensation expense	8,826	10,073
Deferred income tax provision	1,120	1,763
Other	56	2,161
Changes in certain assets and liabilities:		
Accounts receivable	26,047	46,814
Inventories	(28,556)	(31,628)
Accounts payable and accrued liabilities	(23,749)	(89,240)
Accrued income taxes	596	(11,286)
Other	(5,867)	(1,557)
Net cash flow provided by operating activities	44,425	3,138
INVESTING ACTIVITIES		
Purchases of property, plant and equipment	(24,974)	(15,803)
Disposals of property, plant and equipment	148	423
Business acquisitions, net of cash acquired	(17,547)	—
Other	224	(64)
Net cash flow used for investing activities	(42,149)	(15,444)
FINANCING ACTIVITIES		
Net (decrease) increase in notes payable	(38,084)	11,734
Net decrease in short-term revolving and other lines of credit	(3,600)	(15,300)
Term debt borrowings	4,694	267,496
Term debt repayments	(5,000)	(228,478)
Purchase of capital stock	(4,327)	(26,034)
Dividend reinvestment and the effect of employee benefit and stock plans	12,535	2,968
Cash dividends paid to Shareowners	(14,067)	(12,924)
Other	(477)	3,755
Net cash flow (used for) provided by financing activities	(48,326)	3,217
Effect of exchange rate changes on cash and cash equivalents	2,039	3,151
CASH AND CASH EQUIVALENTS		
Net decrease in cash and cash equivalents	(44,011)	(5,938)
Cash and cash equivalents, beginning of period	377,316	116,466
Cash and cash equivalents, end of period	\$333,305	\$110,528

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

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KENNAMETAL INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. ORGANIZATION

From its founding in 1938, the McKenna family incorporated Kennametal Inc. in Pennsylvania in 1943. Kennametal Inc. and its subsidiaries (collectively, Kennametal or the Company) are a leading global manufacturer and supplier of tooling, engineered components and advanced materials consumed in production processes. We believe that our reputation for manufacturing excellence, as well as our technological expertise and innovation we deliver in our products and services, helps us to achieve a leading position in our primary markets. End users of our products include metalworking and machinery manufacturers and suppliers across a diverse array of industries, including the aerospace, defense, transportation, machine tool, light machinery and heavy machinery, as well as producers and suppliers in a number of equipment-intensive industries such as coal mining, road construction and quarrying, as well as oil and gas exploration, refining, production and supply. Our end users' applications range from airframes to mining operations, engines to oil wells and turbochargers to processing. We operate two global business segments consisting of Industrial and Infrastructure.

2. BASIS OF PRESENTATION

The condensed consolidated financial statements, which include our accounts and those of our majority-owned subsidiaries, should be read in conjunction with our 2013 Annual Report on Form 10-K. The condensed consolidated balance sheet as of June 30, 2013 was derived from the audited balance sheet included in our 2013 Annual Report on Form 10-K. These interim statements are unaudited; however, we believe that all adjustments necessary for a fair statement of the results of the interim periods were made and all adjustments are normal adjustments. The results for the three months ended September 30, 2013 and 2012 are not necessarily indicative of the results to be expected for a full fiscal year. Unless otherwise specified, any reference to a "year" is to a fiscal year ended June 30. For example, a reference to 2014 is to the fiscal year ending June 30, 2014. When used in this Form 10-Q, unless the context requires otherwise, the terms "we," "our" and "us" refer to Kennametal Inc. and its subsidiaries.

3. NEW ACCOUNTING STANDARDS**Adopted**

As of July 1, 2013, Kennametal adopted disclosure requirements related to reclassifications out of accumulated other comprehensive income by component. See Note 15 to these condensed consolidated financial statements for required disclosures. Other than the change in disclosures, the adoption of this guidance had no impact on the condensed consolidated financial statements.

As of July 1, 2013, Kennametal adopted additional guidance on testing indefinite lived intangible assets for impairment. The guidance permits an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of an indefinite lived intangible asset is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step impairment test. The adoption of this guidance had no impact on the condensed consolidated financial statements.

4. SUPPLEMENTAL CASH FLOW DISCLOSURES

	Three Months Ended	
	September 30,	
(in thousands)	2013	2012
Cash paid during the period for:		

Interest	\$7,020	\$8,496
Income taxes	7,260	21,247
Supplemental disclosure of non-cash information:		
Changes in accounts payable related to purchases of property, plant and equipment	8,600	—

5. 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. The fair value hierarchy consists of three levels to prioritize the inputs used in valuations, as defined below:

Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

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KENNAMETAL INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, including quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; inputs other than quoted prices that are observable for the asset or liability (e.g., interest rates); and inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3: Inputs that are unobservable.

As of September 30, 2013, the fair values of the Company's financial assets and financial liabilities measured at fair value on a recurring basis are categorized as follows:

(in thousands)	Level 1	Level 2	Level 3	Total
Assets:				
Derivatives ⁽¹⁾	\$—	\$107	\$—	\$107
Total assets at fair value	\$—	\$107	\$—	\$107
Liabilities:				
Derivatives ⁽¹⁾	\$—	\$862	\$—	\$862
Contingent consideration	—	—	14,000	14,000