COMMSCOPE INC
Form 10-Q
November 14, 2001

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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# FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2001

OR

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

For the transition period from ___________ to ___________

Commission file number 001-12929

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

| DELAWARE | 36-4135495 |
|---|---|
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

1375 LENOIR-RHYNE BOULEVARD, P.O. BOX 339
HICKORY, NORTH CAROLINA
(Address of principal executive offices)
28603
(Zip Code)

(828) 324-2200
(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 X No

As of October 31, 2001 there were 51,467,154 shares of Common Stock outstanding.

COMMSCOPE, INC.
FORM 10-Q
SEPTEMBER 30, 2001
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COMMSCOPE, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(UNAUDITED--IN THOUSANDS, EXCEPT NET INCOME PER SHARE AMOUNTS)

| | Three Months Ended September 30, | | Nin S |
|---|---|---|---|
| | 2001 | 2000 | 200 |
| Net sales | $ 177,702 | $ 256,873 | $ |
| Operating costs and expenses: | | | |
| Cost of sales | 133,755 | 190,608 | |
| Selling, general and administrative | 19,019 | 20,105 | |
| Research and development | 1,834 | 5,158 | |
| Amortization of goodwill | 1,340 | 1,341 | |
| Terminated acquisition costs (Note 10) | 9,294 | - | |
| Impairment charges for fixed assets and investments (Note 7) | - | - | |

| | | | |
|---|---|---|---|
| Total operating costs and expenses | 165,242 | 217,212 | |
| Operating income | 12,460 | 39,661 | |
| Other income (expense), net | (472) | 12 | |
| Interest expense | (2,211) | (2,635) | |
| Interest income | 294 | 39 | |
| Income before income taxes | 10,071 | 37,077 | |
| Provision for income taxes | (3,726) | (14,089) | |
| Net income | $ 6,345 | $ 22,988 | $ |
| Net income per share (Note 4): | | | |
| Basic | $ 0.12 | $ 0.45 | $ 0 |
| Assuming dilution | $ 0.12 | $ 0.43 | $ 0 |
| Weighted average shares outstanding (Note 4): | | | |
| Basic | 51,440 | 51,229 | 51, |
| Assuming dilution | 52,350 | 55,972 | 52, |

See notes to condensed consolidated financial statements.



COMMSCOPE, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS, EXCEPT SHARE AMOUNTS)

| | (Unaudited) September 30, 2001 | Dec |
|---|---|---|
| ASSETS | | |
| Cash and cash equivalents | $ 40,928 | $ |
| Accounts receivable, less allowance for doubtful accounts of $13,206 and $9,187, respectively | 144,511 | |
| Inventories (Note 2) | 47,821 | |
| Prepaid expenses and other current assets (Note 7) | 4,734 | |
| Deferred income taxes | 20,146 | |
| Total current assets | 258,140 | |
| Property, plant and equipment, net (Note 7) | 270,447 | |
| Goodwill, net of accumulated amortization of $58,158 and $54,140, respectively | 152,652 | |
| Other intangibles, net of accumulated amortization of $36,765 and $34,796, respectively | 12,000 | |
| Other assets (Notes 6 and 7) | 7,188 | |

| | | |
|---|---|---|
| Total Assets | $ 700,427 | $ |

LIABILITIES AND STOCKHOLDERS' EQUITY

| | | |
|---|---|---|
| Accounts payable | $ 20,730 | $ |
| Other accrued liabilities | 41,855 | |
| Current portion of long-term debt (Note 3) | 2,735 | |
| Total current liabilities | 65,320 | |
| Long-term debt, less current portion (Note 3) | 192,870 | |
| Deferred income taxes | 21,361 | |
| Other noncurrent liabilities | 20,297 | |
| Total Liabilities | 299,848 | |
| Commitments and contingencies (Note 8) | | |
| Stockholders' Equity: | | |
| Preferred stock, $.01 par value; Authorized shares: 20,000,000; Issued and outstanding shares: None at September 30, 2001 and December 31, 2000 | - | |
| Common stock, $.01 par value; Authorized shares: 300,000,000; Issued and outstanding shares: 51,466,154 at September 30, 2001; 51,263,703 at December 31, 2000 | 515 | |
| Additional paid-in capital | 179,030 | |
| Retained earnings | 229,704 | |
| Accumulated other comprehensive loss (Note 5) | (8,670) | |
| Total Stockholders' Equity | 400,579 | |
| Total Liabilities and Stockholders' Equity | $ 700,427 | $ |

See notes to condensed consolidated financial statements.



COMMSCOPE, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED - IN THOUSANDS)

| | Nine Months En<br>September 30 | |
|---|---|---|
| | 2001 | |
| Operating Activities: | | |
| Net income | $ 28,902 | $ |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 30,080 | |

| | | |
|---|---|---|
| Impairment charges for fixed assets and investments | 12,615 | |
| Deferred income taxes | (5,826) | |
| Tax benefit from stock option exercises | 617 | |
| Changes in assets and liabilities: | | |
| Accounts receivable | 52,199 | |
| Inventories | 15,525 | |
| Prepaid expenses and other current assets | (3) | |
| Accounts payable and other accrued liabilities | (15,182) | |
| Other noncurrent liabilities | 3,515 | |
| Other | 72 | |
| Net cash provided by operating activities | 122,514 | |
| Investing Activities: | | |
| Additions to property, plant and equipment | (59,465) | |
| Other | (880) | |
| Net cash used in investing activities | (60,345) | |
| Financing Activities: | | |
| Net borrowings (repayments) under revolving credit facility | (30,000) | |
| Principal payments on long-term debt | (1,326) | |
| Proceeds from exercise of stock options | 2,612 | |
| Net cash provided by (used in) financing activities | (28,714) | |
| Effect of exchange rate changes on cash | (231) | |
| Change in cash and cash equivalents | 33,224 | |
| Cash and cash equivalents, beginning of period | 7,704 | |
| Cash and cash equivalents, end of period | $ 40,928 | $ |

See notes to condensed consolidated financial statements.



COMMSCOPE, INC.
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
AND COMPREHENSIVE INCOME
(UNAUDITED - IN THOUSANDS, EXCEPT SHARE AMOUNTS)

Number of common shares outstanding:
Balance at beginning of period
Issuance of shares for stock option exercises

| | |
|---|---|
| Balance at end of period | |
| **Common stock:** | |
| Balance at beginning of period | $ |
| Issuance of shares for stock option exercises | |
| Balance at end of period | $ |
| **Additional paid-in capital:** | |
| Balance at beginning of period | $ |
| Issuance of shares for stock option exercises | |
| Tax benefit from stock option exercises | |
| Balance at end of period | $ |
| **Retained earnings:** | |
| Balance at beginning of period | $ |
| Net income | |
| Balance at end of period | $ |
| **Accumulated other comprehensive loss:** | |
| Balance at beginning of period | $ |
| Other comprehensive loss | |
| Balance at end of period | $ |
| Total stockholders' equity | $ |

| | Three Months Ended September 30, | |
|---|---|---|
| | 2001 | 2000 |
| **Comprehensive income:** | | |
| Net income | $ 6,345 | $ 22,988 |
| Other comprehensive loss, net of tax (Note 5): | | |
| Foreign currency translation gain (loss) - foreign subsidiaries | 788 | (968) |
| Foreign currency transaction loss on long-term intercompany loans - foreign subsidiaries | (2,490) | (876) |
| Hedging gain (loss) on nonderivative instruments (Note 6) | (617) | 679 |
| Effect of adopting SFAS No. 133 (Note 6) | - | - |
| Loss on derivative financial instruments designated as cash flow hedges (Note 6) | (112) | - |
| Total other comprehensive loss, net of tax | (2,431) | (1,165) |
| Total comprehensive income | $ 3,914 | $ 21,823 |

See notes to condensed consolidated financial statements.

COMMSCOPE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED - IN THOUSANDS, UNLESS OTHERWISE NOTED)

## 1. BACKGROUND AND BASIS OF PRESENTATION

### BACKGROUND

CommScope, Inc. ("CommScope" or the "Company"), through its wholly owned subsidiaries, operates in the cable manufacturing business. CommScope is a leading worldwide designer, manufacturer and marketer of a wide array of broadband coaxial cables and other high-performance electronic and fiber optic cable products for cable television, telephony, Internet access and wireless communications. Management believes CommScope is the world's largest manufacturer of coaxial cable for hybrid fiber coax (HFC) cable television systems. CommScope is also a leading supplier of coaxial, twisted pair, and fiber optic cables for premise wiring (local area networks), wireless and other communication applications.

### BASIS OF PRESENTATION

The condensed consolidated balance sheet as of September 30, 2001, the condensed consolidated statements of income and comprehensive income for the three and nine months ended September 30, 2001 and 2000 and the condensed consolidated statements of cash flows and stockholders' equity for the nine months ended September 30, 2001 and 2000 are unaudited and reflect all adjustments of a normal recurring nature which are, in the opinion of management, necessary for a fair presentation of the interim period financial statements. The results of operations for the interim period are not necessarily indicative of the results of operations to be expected for the full year.

The unaudited interim condensed consolidated financial statements of CommScope have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. These interim condensed consolidated financial statements should be read in conjunction with the Company's December 31, 2000 audited consolidated financial statements and notes thereto included in the Company's 2000 Annual Report on Form 10-K.

### GOODWILL

When events or changes in circumstances, such as significant forecasted operating losses or a significant adverse change in legal factors or business climate, indicate that the carrying amount of goodwill may not be recoverable, the asset is reviewed by management for impairment. An impairment loss is recognized if the carrying value exceeds the forecasted, undiscounted operating cash flows of the operating assets related to the goodwill being evaluated. The impairment loss to be recognized is measured as the amount by which the carrying value exceeds

fair value, estimated based on forecasted operating cash flows, discounted using a discount rate commensurate with the risks involved. After the impairment loss is recognized, the reduced carrying amount is accounted for as the new cost and amortized over the remaining useful life, which is also revised, if appropriate. There were no events or changes in circumstances during the three and nine months ended September 30, 2001 that would indicate that the carrying amount of goodwill may not be recoverable (see Note 11 for Impact of Newly Issued Accounting Standards).

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(UNAUDITED - IN THOUSANDS, UNLESS OTHERWISE NOTED)

SHIPPING AND HANDLING COSTS

Amounts billed to a customer in a sale transaction related to shipping costs are included in net sales. All shipping costs incurred to transport products to the customer are recorded in cost of sales. Internal handling costs, which relate to activities to prepare goods for shipment, are recorded in selling, general and administrative expense and were not material for the three and nine months ended September 30, 2001 or 2000.

2. INVENTORIES

| | September 30, 2001 | December 31, 2000 |
|---|---|---|
| Raw materials | $ 21,932 | $ 28,382 |
| Work in process | 12,874 | 11,124 |
| Finished goods | 13,015 | 24,257 |
| | $ 47,821 | $ 63,763 |

3. LONG-TERM DEBT

| | September 30, 2001 | December 31, 2000 |
|---|---|---|
| Credit Agreement | $ -- | $ 30,000 |
| Convertible Notes | 172,500 | 172,500 |
| Eurodollar Credit Agreement | 12,305 | 14,136 |
| IDA Notes | 10,800 | 10,800 |
| | 195,605 | 227,436 |
| Less current portion | (2,735) | (2,120) |
| | $ 192,870 | $ 225,316 |

4. NET INCOME PER SHARE

Basic net income per share is computed by dividing net income by the weighted average number of common shares outstanding during the applicable

periods. Diluted net income per share is based on net income adjusted for after-tax interest and amortization of debt issuance costs related to convertible debt, if dilutive, divided by the weighted average number of common shares outstanding adjusted for the dilutive effect of stock options and convertible securities. The diluted net income per share calculation assumes the exercise of stock options using the treasury stock method.



NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(UNAUDITED - IN THOUSANDS, UNLESS OTHERWISE NOTED)

Below is a reconciliation of weighted average common shares outstanding for basic net income per share to weighted average common and potential common shares outstanding for diluted net income per share.

| | Three Months Ended September 30, | | Nine Months End September 30, | |
|---|---|---|---|---|
| | 2001 | 2000 | 2001 | 20 |
| NUMERATOR: | | | | |
| Net income for basic net income per share | $ 6,345 | $ 22,988 | $ 28,902 | $ |
| Convertible debt interest and amortization, net of tax | -- | 1,177 | -- | |
| Net income available to common stock-holders for diluted net income per share | $ 6,345 | $ 24,165 | $ 28,902 | $ |
| DENOMINATOR: | | | | |
| Weighted average number of common shares outstanding for basic net income per share | 51,440 | 51,229 | 51,384 | |
| Effect of dilutive securities: | | | | |
| Convertible debt (A) | -- | 3,580 | -- | |
| Employee stock options (B) | 910 | 1,163 | 824 | |
| Weighted average number of common and potential common shares outstanding for diluted net income per share | 52,350 | 55,972 | 52,208 | |



NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED - IN THOUSANDS, UNLESS OTHERWISE NOTED)

5. INCOME TAXES RELATED TO OTHER COMPREHENSIVE INCOME

| | Three Months Ended September 30, | | Nine Months September |
|---|---|---|---|
| | 2001 | 2000 | 2001 |
| Income tax benefit (expense) for components of other comprehensive income: | | | |
| Hedging loss (gain) on nonderivative instruments | $ 397 | $(416) | $(164) |
| Effect of adopting SFAS No. 133 | -- | -- | (135) |
| Loss on derivative instruments designated as cash flow hedges | 66 | -- | 122 |
| Total income tax benefit (expense) for components of other comprehensive income | $ 463 | $(416) | $(177) |

6. DERIVATIVES AND HEDGING ACTIVITIES UNDER SFAS NO. 133

Effective January 1, 2001, the Company adopted Statement of Financial Accounting Standards ("SFAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended by SFAS No. 137, "Accounting for Derivative Instruments and Hedging Activities--Deferral of the Effective Date for FASB Statement No. 133" and SFAS No. 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities." SFAS No. 133, as amended, establishes accounting and reporting standards for derivative financial instruments, including certain derivative instruments embedded in other host contracts (collectively referred to as embedded derivatives) and for hedging activities. The new standards require an entity to recognize all derivatives as either assets or liabilities in the balance sheet and measure those instruments at fair value.

CommScope is exposed to various risks resulting from adverse fluctuations in commodity prices, interest rates, and foreign currency exchange rates. CommScope's risk management strategy includes the use of derivative and nonderivative financial instruments primarily as hedges of these risks in accordance with the requirements of SFAS No. 133, whenever management determines their use to be reasonable and practical. This strategy does not permit the use of derivative financial instruments for trading purposes, nor does it allow for speculation. A hedging instrument may be designated as a fair value hedge to manage exposure to risks related to a firm commitment for the purchase of raw materials or a foreign-currency-denominated firm commitment for the purchase of equipment, or it may be designated as a cash flow hedge to manage exposure to risks related to a forecasted purchase of raw materials, variable interest rate payments, or a forecasted foreign-currency-denominated sale of product. In addition, the use of nonderivative financial instruments is limited to hedging fair value risk related to a foreign-currency-denominated firm commitment or a net investment in a foreign subsidiary.

The Company's risk management strategy permits the reasonable and practical use of derivative hedging instruments such as forward contracts,

options, cross currency swaps, certain interest rate swaps, caps and floors, and nonderivative hedging instruments such as foreign-currency-denominated loans. All hedging instruments are designated and documented, in accordance with SFAS No. 133, as either a fair value hedge, a cash flow hedge or a foreign currency hedge at inception. The effectiveness of designated hedging relationships is tested and documented



NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(UNAUDITED - IN THOUSANDS, UNLESS OTHERWISE NOTED)

on at least a quarterly basis. Any ineffectiveness of cash flow or foreign currency hedges is recognized currently in earnings.

The only derivative instrument identified in the implementation of SFAS No. 133 and outstanding for the three and nine months ended September 30, 2001 was an interest rate swap, which effectively converts the variable-rate Eurodollar Credit Agreement to a fixed-rate basis. As of January 1, 2001, this interest rate swap was designated and documented as a cash flow hedge of the risk of changes in the cash flows attributable to fluctuations in the variable benchmark interest rate associated with the underlying debt being hedged. This hedging instrument was effective at the transition date to SFAS No. 133, and at the balance sheet date, and is expected to continue to be effective for the duration of the swap contract, resulting in no anticipated hedge ineffectiveness and no material reclassifications from other comprehensive income to earnings during the next twelve months. In addition, there were no material reclassification adjustments during the three and nine months ended September 30, 2001. The transition adjustment as of January 1, 2001 was recorded as a change in accounting principle to accumulated other comprehensive loss and other assets on the balance sheet and did not have a material impact on the Company's consolidated results of operations, financial position, and cash flows.

Also, as of January 1, 2001, the Eurodollar Credit Agreement was designated and documented as a hedge of the Company's net investment in its Belgian subsidiary. There was no adjustment required under SFAS No. 133 as of January 1, 2001 related to this net investment hedge. This hedging instrument was effective at the SFAS No. 133 transition date, and at the balance sheet date, and is expected to continue to be effective for the duration of the loan agreement, resulting in no anticipated reclassifications from other comprehensive income to earnings. In addition, the Company does not currently intend to repatriate the earnings of this subsidiary in the foreseeable future.

Activity in the accumulated net gain on derivative instruments included in accumulated other comprehensive loss for the three and nine months ended September 30, 2001 consisted of the following:

| | Three Months Ended Sept 30, 2001 | Nine Months Ended Sept 30 2001 |
|---|---|---|

| | | |
|---|---|---|
| Accumulated net gain on derivative instruments, beginning of period | $ 134 | $ - |
| Net effect of adopting SFAS No. 133 | -- | 22 |
| Net loss on derivative financial instruments designated as cash flow hedges | (112) | (20 |
| Accumulated net gain on derivative instruments, end of period | $ 22 | $ 2 |

7. IMPAIRMENT CHARGES FOR FIXED ASSETS AND INVESTMENTS

The Company has taken a number of steps to closely manage costs and has been evaluating all aspects of its business in response to challenging industry conditions. As a result of its review, the Company recorded pretax impairment charges totaling $12.6 million during the second quarter of 2001. Included in these impairment charges was approximately $3.6 million related to an investment in an unconsolidated affiliate, $4.4 million

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(UNAUDITED - IN THOUSANDS, UNLESS OTHERWISE NOTED)

related to fixed assets identified as held for disposal and $4.6 million related to fixed assets to be held and used.

Management determined that the fair value of the Company's investment in an unconsolidated affiliate was less than its carrying value, which has been accounted for under the cost method. This determination was based on reduced cash flow projections. The fair value of this investment was determined using present value techniques based on anticipated cash flows.

The assets held for disposal consisted of machinery and equipment used or purchased for use in production. Management identified specific assets that were determined to have no future use to the Company and developed a plan of disposal for each of the assets. The assets held for disposal had a carrying value of $1.6 million as of June 30, 2001, after the second quarter impairment charges including costs of disposal. Assets valued at $840 thousand were sold during the third quarter of 2001, leaving a remaining carrying value of $775 thousand, which was included in other current assets as of September 30, 2001.

The assets to be held and used consisted of the Kings Mountain facility, which was under construction, and other machinery and equipment whose anticipated future cash flows have been affected by challenging industry conditions. Although we have not classified this facility as held for disposal, we are uncertain as to its future use. Equipment that was intended for the Kings Mountain facility is expected to be redeployed overseas. The fair values of the assets to be held and used were determined using appraisals or present value techniques.

8. COMMITMENTS AND CONTINGENCIES

As of September 30, 2001, the Company had committed funds of

approximately $4.9 million under purchase orders and contracts for completion of existing capacity related projects.

9. SUPPLEMENTAL CASH FLOW INFORMATION

| | Nine Months Ended September 30, | |
|---|---|---|
| | 2001 | 2000 |
| Cash paid during the period for: | | |
| Income Taxes | $ 17,927 | $ 32,917 |
| Interest | 4,853 | 5,355 |

10. TERMINATED ACQUISITION COSTS

The Company announced on July 24, 2001 that it had agreed with the Furukawa Electric Co., Ltd. of Japan to form two joint ventures to acquire certain fiber cable and transmission fiber assets of the Optical Fiber Solutions Group of Lucent Technologies, Inc. Given the uncertain economic environment and severe downturn in the telecommunications market as well as associated difficulties in the financing markets following the September 11th tragedy, CommScope is in discussions with Furukawa to restructure the joint venture arrangements. The Company expects to reduce its investment and participation in the joint ventures due to the potential restructuring.





As a result of the restructuring discussions, the Company recorded pretax charges of approximately $9.3 million, or approximately $0.11 per diluted share, net of tax, during the three months ended September 30, 2001, related to financing and formation costs of the original joint venture arrangements.

11. IMPACT OF NEWLY ISSUED ACCOUNTING STANDARDS

In July 2001, the Financial Accounting Standards Board ("FASB") issued SFAS No. 141, "Business Combinations" and SFAS No. 142, "Goodwill and Other Intangible Assets." Both statements are effective for the Company on January 1, 2002, except that business combinations, including related goodwill and intangible assets, occurring after June 30, 2001 are immediately subject to the provisions of the two Statements. SFAS No. 141 requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001 and broadens the criteria for recording intangible assets separate from goodwill. SFAS No. 142 requires the use of a nonamortization approach to account for purchased goodwill and certain intangible assets with indefinite useful lives and also requires at least an annual assessment for impairment by applying a fair-value-based test. Goodwill and certain intangible assets with indefinite lives acquired after June 30, 2001 are immediately subject to the nonamortization provisions of SFAS No. 142. Intangible assets with definite useful lives will continue to be amortized over their useful lives. The adoption of these statements will have a material impact on the Company's results of

operations and financial position after January 1, 2002 when goodwill will no longer be amortized. The pretax impact on the Company's results of operations and financial position of adopting a nonamortization approach to accounting for goodwill under SFAS No. 142 is expected to be approximately $5.3 million per year. The Company is currently assessing the impact of the other provisions of these two statements, which will be adopted on January 1, 2002.

In August 2001, the FASB issued SFAS No. 143, "Accounting for Obligations Associated with the Retirement of Long-Lived Assets." SFAS No. 143 will require the accrual, at fair value, of the estimated retirement obligation for tangible long-lived assets if the Company is legally obligated to perform retirement activities at the end of the related asset's life. The Company is currently assessing the impact of this statement, which will be effective for the Company on January 1, 2003.

In October 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," which supersedes SFAS No. 121, "Accounting for the Impairment or Disposal of Long-Lived Assets and for Long-Lived Assets to be Disposed Of," but retains many of its fundamental provisions. Additionally, this statement expands the scope of discontinued operations to include more disposal transactions. The Company is currently assessing the impact of this statement, which will be effective for the Company on January 1, 2002.



ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis is provided to increase the understanding of, and should be read in conjunction with, the unaudited condensed consolidated financial statements and accompanying notes included in this document as well as the audited consolidated financial statements, related notes thereto and management's discussion and analysis of financial condition and results of operations for the year ended December 31, 2000 included in our Annual Report on Form 10-K.

HIGHLIGHTS

Net income was $6 million, or $0.12 per diluted share, for the quarter ended September 30, 2001 compared to net income of $23 million, or $0.43 per diluted share for the quarter ended September 30, 2000. Net income for the current quarter included charges of approximately $0.11 per diluted share, net of tax, related to terminated acquisition costs (see further discussion below).

Net income was $29 million, or $0.55 per diluted share, for the nine months ended September 30, 2001 compared to net income of $62 million, or $1.17 per diluted share, for the nine months ended September 30, 2000. Net income for the nine months ended September 30, 2001 included charges of approximately $0.26 per diluted share, net of tax, related to terminated acquisition costs and impairment charges for fixed assets and investments. An ongoing global slowdown in the telecommunications industry, as well as second quarter impairment charges and third quarter terminated acquisition costs contributed to the decline in earnings.

COMPARISON OF RESULTS OF OPERATIONS FOR THE THREE MONTHS AND NINE MONTHS

ENDED SEPTEMBER 30, 2001 WITH THE THREE MONTHS AND NINE MONTHS ENDED SEPTEMBER 30, 2000

Net Sales

Net sales for the third quarter ended September 30, 2001 decreased $79 million, or 31%, to $178 million, compared to the third quarter ended September 30, 2000. Net sales for the nine months ended September 30, 2001 decreased $107 million, or 15%, to $595 million, compared to the nine months ended September 30, 2000. Revenues reflect an ongoing global slowdown in telecommunications spending. We expect these challenging business conditions to continue to affect our performance and, currently expect sales in the fourth quarter of 2001 to be down 10-20% sequentially.

Domestic sales decreased 27% to $143 million in the third quarter and 14% to $455 million in the nine months ended September 30, 2001, compared to the same periods in 2000. For the third quarter of 2001, international sales decreased 42% to $34 million compared to the same period in 2000. International sales and orders were down year over year in all regions. International sales for the nine months ended September 30, 2001 decreased 18% to $140 million compared to the same period in 2000.

Net sales to broadband and other video distribution markets ("Broadband/Video Products") for the third quarter of 2001 decreased $55 million, or 28%, to $139 million, from the same period in 2000. For the nine months ended September 30, 2001, net sales of Broadband/Video Products decreased $52 million, or 10%, to $469 million, from the same period in 2000. We have not changed the composition of this product group, but have changed the name from CATV/Video to Broadband/Video in order to reflect the ongoing convergence of video, voice and data. The year-over-year decrease in net sales of Broadband/Video products was primarily due to lower coaxial cable volume, which was somewhat offset by higher sales of fiber optic cable. Sales of fiber optic cable represented more than 15% of total worldwide sales in the third quarter ended September 30, 2001, primarily for Broadband/Video applications. Coaxial cable pricing remained generally firm during the third quarter ended September 30, 2001. Third quarter domestic Broadband/Video sales decreased 22%, year over year, despite an increase in fiber optic cable sales which offset a significant decrease in broadband cable sales to AT&T and alternate service providers. The ongoing slowdown in telecommunications as well as the uncertain global economic conditions continues to affect Broadband/Video sales. However, we believe that our ability to offer both coaxial and fiber optic cable continues to be an important competitive advantage over the longer term.



Net sales for local area network and other data applications ("LAN Products") for the third quarter of 2001 increased by $2 million, or 11%, to $23 million, from the same period in 2000. For the nine months ended September 30, 2001, sales of LAN Products increased by $3 million, or 4%, compared to the same period in 2000. The year over year increases in sales of LAN Products were primarily driven by higher volume. However, we expect sales of LAN Products to encounter increasing price pressures in the fourth quarter.

Net sales for wireless and other telecommunications products ("Wireless and Other Telecom Products") for the third quarter of 2001 were $15 million compared to $42 million in the same period last year. For the nine months ended September 30, 2001, sales of Wireless and Other Telecom

Products were $53 million compared to $110 million in the same period last year. The decrease in sales of Wireless and Other Telecom Products was primarily driven by lower volume. Sales of Other Telecom Products, which primarily represent coaxial cables designed for switching and transmission applications for enhanced telecommunications services, accounted for the majority of the decline due to lower capital spending for telephone central office applications and significant competitive pressure.

Gross Profit (Net Sales Less Cost of Sales)

Gross profit for the third quarter ended September 30, 2001 was $44 million, compared to third quarter 2000 gross profit of $66 million, and third quarter gross profit margin declined to 24.7% from 25.8%, year over year. For the nine months ended September 30, 2001, gross profit decreased to $145 million, compared to $183 million for the same period in 2000 with gross profit margins of 24.4% and 26.1%, respectively. The decline in gross profit margins was primarily due to lower sales volumes, increased overhead costs associated with capacity expansion and shifting product mix. We intend to continue evaluating all aspects of our business and closely manage costs. However, despite these efforts, we expect margin compression during the fourth quarter of 2001, primarily as a result of lower sales volumes, shifting product mix, and lower prices for certain products.

Selling, General and Administrative

Selling, general and administrative ("SG&A") expense for the third quarter ended September 30, 2001 was $19 million, or 11% of net sales, compared to $20 million, or 8% of net sales, for the same period in 2000. The year-over-year decrease in SG&A expense in the third quarter was offset by a more significant decrease in sales, resulting in an increase in SG&A expense as a percentage of net sales. For the nine months ended September 30, 2001, SG&A expense was $62 million, or 10% of sales, compared to $59 million, or 8% of sales, for the same period in 2000. The year-over-year increase in SG&A expense as a percentage of sales for the nine months ended September 30, 2001 was mainly due to the decrease in sales and an increase in bad debt expense resulting from a more difficult collection environment.



Research and Development

Research and development ("R&D") expense decreased to $2 million, or 1% of net sales, for the third quarter ended September 30, 2001 from $5 million, or 2% of net sales, for the same period in 2000. For the nine months ended September 30, 2001, R&D expense decreased to $5 million, or 1% of sales, compared to $14 million, or 2% of sales, for the same period in 2000. These decreases were primarily due to the substantial completion of certain vertical integration projects for bimetallic wire fabrication and fine wire drawing. We have ongoing programs to develop new products and market opportunities for our products and core capabilities and new manufacturing technologies to achieve cost reductions.

Terminated Acquisition Costs

We announced on July 24, 2001 that we had agreed with the Furukawa Electric Co., Ltd. of Japan to form two joint ventures to acquire certain fiber cable and transmission fiber assets of the Optical Fiber Solutions Group of Lucent Technologies, Inc. Given the uncertain economic environment and severe downturn in the telecommunications market as well as associated

difficulties in the financing markets following the September 11th tragedy, management is in discussions with Furukawa to restructure the joint venture arrangements. We expect to reduce our investment and participation in the joint ventures due to the potential restructuring. As a result of the restructuring discussions, we recorded pretax charges of approximately $9 million, or $0.11 per diluted share, net of tax, during the three months ended September 30, 2001, related to financing and formation costs of the original joint venture arrangements and we expect to incur additional charges of $800 thousand, net of tax, during the fourth quarter of 2001.

Impairment Charges for Fixed Assets and Investments

As previously stated, we have taken a number of steps to closely manage costs and have been evaluating all aspects of our business in response to challenging industry conditions. As a result of our review, we recorded pretax charges of approximately $13 million, or $0.15 per diluted share, net of tax, during the nine months ended September 30, 2001 related to the impairment of certain assets. Management identified specific assets that were determined to have no future use in our operations and assets whose anticipated future cash flows have fallen below their book values. These adjustments included equipment charges and a write-down of the Kings Mountain facility, which was under construction. Equipment that was intended for the Kings Mountain facility is expected to be redeployed overseas. The write-off of an investment in an unconsolidated affiliate, whose fair value was determined to be less than its carrying value due to reduced cash flow projections, was also included in the charges.

Net Interest Expense

Net interest expense for the third quarter ended September 30, 2001 decreased to $1.9 million, compared to $2.6 million for the same period in 2000. For the nine months ended September 30, 2001, net interest expense decreased to $5.6 million, compared to $7.1 million for the same period in 2000. The decrease in net interest expense was primarily due to a lower long-term debt balance at September 30, 2001, compared to September 30, 2000.

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Income Taxes

Our effective tax rate was 37% for the third quarter and nine months ended September 30, 2001, compared to 38% for the same periods in 2000. This decrease in our effective tax rate was mainly due to specific tax savings strategies implemented late in 2000.

LIQUIDITY AND CAPITAL RESOURCES

Cash provided by operating activities was $123 million for the nine months ended September 30, 2001, compared to $33 million for the same period in 2000. This year-over-year increase in operating cash flow primarily resulted from reduced working capital on lower sales volume.

Working capital was $193 million at September 30, 2001, compared to $209 million at December 31, 2000. The decrease primarily relates to lower accounts receivable due to declining sales. We believe that working capital levels are appropriate to support current levels of orders and backlog. We had an order backlog of approximately $39 million as of September 30, 2001, compared to $156 million as of December 31, 2000. Orders typically

fluctuate from quarter to quarter based on customer demand and general business conditions. In some cases, unfilled orders may be cancelled prior to shipment of goods. Backlog includes only orders for products scheduled to be shipped within six months.

During the nine months ended September 30, 2001, we invested $59 million in property, plant and equipment compared to $79 million during the same period in 2000. As of September 30, 2001, we had committed funds of nearly $5 million under purchase orders and contracts for completion of existing capacity related projects. In response to current market conditions, we intend to continue evaluating all aspects of our business, including the timing and location of capacity needs. We expect capital expenditures for equipment and facilities in 2001 to be approximately $70-$80 million, with the majority of funds invested in global capacity expansion projects. We currently expect capital expenditures to be in the range of $30-$40 million in 2002, depending upon business conditions.

Our principal sources of liquidity both on a short-term and long-term basis are cash flows provided by operations and funds available under long-term credit facilities. We currently have $350 million of available borrowing capacity under our revolving credit agreement, which expires in December 2002. We owed long-term debt of $196 million, or 33% of our book capital structure, defined as long-term debt and total stockholders' equity, as of September 30, 2001, compared to $227 million, or 38% of our book capital structure as of December 31, 2000. The decrease in long-term debt was due to the repayment of $30 million under our revolving credit agreement and the first two quarterly principal payments and favorable impact of foreign exchange rate fluctuations on our 15 million eurodollar term loan.

Based upon our analysis of our consolidated financial position and the expected results of our operations in the future, we believe that we will have sufficient cash flows from future operations and the financial flexibility to attract both short-term and long-term capital on acceptable terms as may be needed to fund operations, capital expenditures and other currently anticipated growth objectives. There can be no assurance, however, that future industry-specific developments, general economic trends or other situations will not adversely affect our operations or ability to meet cash requirements.



MARKET RISK

Effective January 1, 2001, we adopted Statement of Financial Accounting Standards ("SFAS") No. 133, "Accounting for Derivative Financial Instruments and Hedging Activities," as amended by SFAS Nos. 137 and 138. The adoption of SFAS No. 133, as amended, did not have a material impact on our consolidated results of operations, financial position, and cash flows as of January 1, 2001. SFAS No. 133 establishes accounting and reporting standards for derivative financial instruments, including certain derivative instruments embedded in other host contracts and for hedging activities.

As disclosed in our Annual Report on Form 10-K for the year ended December 31, 2000, our major market risk exposure relates to adverse fluctuations in commodity prices, interest rates and foreign currency exchange rates. We have established a risk management strategy that includes the use of derivative and nonderivative financial instruments

primarily to manage our exposure to these market risks in accordance with the requirements of SFAS No. 133, whenever management determines their use to be reasonable and practical. Our exposure associated with these market risks has not materially changed since December 31, 2000. However, we did repay $30 million of variable rate debt on our revolving credit agreement in the first quarter of 2001 and approximately $1 million of variable rate debt on our Eurodollar Credit Agreement, somewhat reducing our exposure to interest rate risk. In addition, we have not acquired any new derivative financial instruments since December 31, 2000 or terminated any derivative financial instruments that existed at that date.

FORWARD-LOOKING STATEMENTS

Certain statements in this Form 10-Q that are other than historical facts are intended to be "forward-looking statements" within the meaning of the Securities Exchange Act of 1934, the Private Securities Litigation Reform Act of 1995 and other related laws and include but are not limited to those statements relating to sales and earnings expectations, expected demand, cost and availability of key raw materials, internal production capacity and expansion, competitive pricing, relative market position and outlook. While we believe such statements are reasonable, the actual results and effects could differ materially from those currently anticipated. These forward-looking statements are identified, including, without limitation, by their use of such terms and phrases as "intends," "intend," "intended," "goal," "estimate," "estimates," "expects," "expect," "expected," "project," "projects," "projected," "projections," "plans," "anticipates," "anticipated," "should," "designed to," "foreseeable future," "believe," "believes," "think," "thinks" and "scheduled" and similar expressions. These statements are subject to various risks and uncertainties, many of which are outside our control, including, without limitation, expected demand from our customers, cost and availability of key raw materials (including without limitation bimetallic center conductors, optical fibers, fine aluminum wire and fluorinated-ethylene-propylene which are available only from limited sources), successful implementation of internal bimetal production and other vertical integration activities, pricing and acceptance of our products, successful expansion and related operation of our facilities, conditions of excess capacity, the ability to implement cost reductions in a timely manner and the success of those actions, margin improvement, developments in technology, industry competition, achievement of sales, growth, and earnings goals, ability of our customers to secure adequate financing, regulatory changes affecting our business, worldwide economic conditions, foreign currency fluctuations, technological obsolescence, the ability to integrate acquisitions, international economic and political

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uncertainties and other factors discussed. Actual results may also differ due to changes in communications industry capital spending, which is affected by a variety of factors, including, without limitation, general economic conditions, acquisitions of communications companies by others, consolidation within the communications industry, the financial condition of communications companies and their access to financing, competition among communications companies, technological developments, and new legislation and regulation of communications companies. These and other factors are discussed in greater detail in Exhibit 99 to this Form 10-Q. The information contained in this Form 10-Q represents our best judgment at the date of this report based on information currently available. However,

we do not intend to update this information to reflect developments or information obtained after the date of this report and are not undertaking any duty or obligation to do so.



PART II - OTHER INFORMATION

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

EXHIBIT NO.

99. Forward-Looking Information

(b) Reports on Form 8-K filed during the three months ended September 30, 2001:

On July 24, 2001 we filed a current report on Form 8-K announcing our second quarter 2001 results and an agreement with The Furukawa Electric Co., Ltd. of Japan to form two joint ventures to acquire certain fiber cable and transmission fiber assets of the Optical Fiber Solutions Group of Lucent Technologies Inc.



SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

COMMSCOPE, INC.

| November 14, 2001 | /s/ Jearld L. Leonhardt |
| --- | --- |
| Date | Jearld L. Leonhardt<br>Executive Vice President and Chief Financial Officer<br>Signing both in his capacity as Executive Vice President on behalf of the Registrant and as Chief Financial Officer of the Registrant |