

MATERIAL SCIENCES CORP
Form 10-Q
July 10, 2008

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 May 31, 2008

Commission File Number 1-8803

MATERIAL SCIENCES CORPORATION

(Exact name of Registrant as specified in its charter)

Delaware
(State or other jurisdiction
of incorporation or organization)

2200 East Pratt Boulevard

95-2673173
(IRS employer
identification number)

60007

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Elk Grove Village, Illinois
(Address of principal executive offices)

(Zip code)

Registrant's telephone number, including area code: (847) 439-2210

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 is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller Reporting Company

(Do not check if a smaller reporting company)

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 June 30, 2008, there were 13,763,566 outstanding shares of common stock, \$.02 par value.

MATERIAL SCIENCES CORPORATION

FORM 10-Q

For the Quarter Ended May 31, 2008

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

- (a) Financial statements of Material Sciences Corporation and Subsidiaries

Condensed Consolidated Statements of Operations (Unaudited)

Material Sciences Corporation and Subsidiaries

(In thousands, except per share data)	Three Months Ended May 31,	
	2008	2007
Net Sales	\$ 57,165	\$ 60,665
Cost of Sales	50,364	51,944
Gross Profit	6,801	8,721
Selling, General and Administrative Expenses	10,354	10,288
Loss from Operations	(3,553)	(1,567)
Other Income, Net :		
Interest Income, Net	(74)	(82)
Equity in Results of Joint Venture	(81)	(56)
Other, Net	(490)	(517)
Total Other Income, Net	(645)	(655)
Loss from Operations Before Benefit for Income Taxes	(2,908)	(912)
Benefit for Income Taxes	(1,336)	(367)
Net Loss	\$ (1,572)	\$ (545)
Basic Net Loss Per Share	\$ (0.11)	\$ (0.04)
Diluted Net Loss Per Share	\$ (0.11)	\$ (0.04)
Weighted Average Number of Common Shares Outstanding Used for Basic Net Loss Per Share	13,856	14,531
Dilutive Shares		
Weighted Average Number of Common Shares Outstanding Plus Dilutive Shares	13,856	14,531
Outstanding Common Stock Options Having No Dilutive Effect	372	199

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

Condensed Consolidated Balance Sheets (Unaudited)

Material Sciences Corporation and Subsidiaries

(In thousands)	May 31, 2008	February 28, 2008
Assets:		
Current Assets:		
Cash and Cash Equivalents	\$ 10,801	\$ 7,913
Short Term Investments	4,132	6,933
Receivables, Less Reserves of \$2,822 and \$3,708, Respectively	29,723	28,547
Income Taxes Receivable	3,013	3,316
Prepaid Expenses	1,747	744
Inventories	29,579	31,811
Deferred Income Taxes	3,287	3,754
Assets Held for Sale	3,882	3,882
Other Assets	175	180
Total Current Assets	86,339	87,080
Property, Plant and Equipment	215,250	213,842
Accumulated Depreciation, Amortization and Accretion	(149,273)	(146,541)
Net Property, Plant and Equipment	65,977	67,301
Other Assets:		
Investment in Joint Venture	3,308	3,094
Deferred Income Taxes	8,730	6,608
Other	345	232
Total Other Assets	12,383	9,934
Total Assets	\$ 164,699	\$ 164,315
Liabilities:		
Current Liabilities:		
Accounts Payable	\$ 26,645	\$ 22,513
Accrued Payroll Related Expenses	4,445	4,691
Accrued Expenses	7,575	7,403
Total Current Liabilities	38,665	34,607
Long-Term Liabilities:		
Pension and Postretirement Liabilities	9,348	9,628
Other	5,722	4,948
Total Long-Term Liabilities	15,070	14,576
Commitments and Contingencies		
Shareowners' Equity:		
Preferred Stock		
Common Stock	381	381
Additional Paid-In Capital	79,582	79,491
Treasury Stock at Cost	(55,684)	(52,978)
Retained Earnings	86,700	88,272

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Accumulated Other Comprehensive Income	(15)	(34)
Total Shareowners' Equity	110,964	115,132
Total Liabilities and Shareowners' Equity	\$ 164,699	\$ 164,315

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

Condensed Consolidated Statements of Cash Flows (Unaudited)

Material Sciences Corporation and Subsidiaries

(In thousands)	Three Months Ended May 31,	
	2008	2007
Cash Flows From:		
Operating Activities:		
Net Income (Loss)	\$ (1,572)	\$ (545)
Adjustments to Reconcile Net Income (Loss) to Net Cash Provided by Operating Activities:		
Depreciation, Amortization and Accretion	2,680	2,911
Provision for Deferred Income Taxes	(1,705)	
Compensatory Effect of Stock Plans	91	34
Foreign Currency Transaction Gain	(354)	(413)
Other, Net	(81)	(25)
Changes in Assets and Liabilities:		
Receivables	(1,116)	16,718
Income Taxes Receivable	303	(474)
Prepaid Expenses	(1,001)	(647)
Inventories	2,295	(5,901)
Accounts Payable	4,540	(9,369)
Accrued Expenses	(112)	(460)
Other, Net	479	(398)
Net Cash Provided by Continuing Operations	4,447	1,431
Net Cash Provided by Discontinued Operations		15
Net Cash Provided by Operating Activities	4,447	1,446
Investing Activities:		
Capital Expenditures	(1,639)	(1,763)
Proceeds from Sale of Marketable Securities	2,800	
Net Cash Provided by (Used in) Investing Activities	1,161	(1,763)
Financing Activities:		
Purchases of Treasury Stock	(2,706)	(278)
Net Cash Used in Financing Activities	(2,706)	(278)
Effect of Exchange Rate Changes on Cash	(14)	11
Net Increase (Decrease) in Cash	2,888	(584)
Cash and Cash Equivalents at Beginning of Period	7,913	11,667
Cash and Cash Equivalents at End of Period	\$ 10,801	\$ 11,083
Non-Cash Transactions:		
Capital Expenditures in Accounts Payable at End of Period	\$ 461	\$ 404
Supplemental Cash Flow Disclosures:		
Interest Paid	\$ 26	\$ 61
Income Taxes Paid	8	319

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

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

MATERIAL SCIENCES CORPORATION and SUBSIDIARIES

The data as of May 31, 2008 and for the three months ended May 31, 2008 and 2007 has not been audited by our independent registered public accounting firm. In the opinion of Material Sciences Corporation (the Company, we, our, us or MSC), the data reflects all adjustments (consisting of only normal, recurring adjustments) necessary for a fair presentation of the information at those dates and for those periods. The financial information contained in this report should be read in conjunction with the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission on May 29, 2008 for the fiscal year ended February 29, 2008.

- (1) **Joint Venture.** In November 2000, a subsidiary of MSC formed a joint venture with Tekno S.A. (Tekno) for the manufacture and sale of Quiet Steel® and disc brake noise damper material for the South American market. The Company includes its portion of the joint venture's results in the Condensed Consolidated Statements of Operations under Equity in Results of Joint Venture. The Equity in Results of Joint Venture was income of \$81,000 for the three months ended May 31, 2008, compared with \$56,000 for the same period in 2007.
- (2) **Preferred Stock.** Preferred Stock, \$1.00 Par Value; 10,000,000 Shares Authorized; 1,000,000 Designated Series B Junior Participating Preferred; None Issued.
- (3) **Common Stock.** Common Stock, \$.02 Par Value; 40,000,000 Shares Authorized; 19,039,817 Shares Issued and 13,773,766 Shares Outstanding as of May 31, 2008 and 19,039,817 Shares Issued and 14,137,566 Shares Outstanding as of February 29, 2008.
- (4) **Treasury Stock.** In February 2006, the Company's Board of Directors authorized the repurchase of up to one million shares of common stock. The shares were repurchased from time-to-time on the open market, and such repurchases were generally funded with internally generated cash. During the fiscal year ended February 28, 2007, the Company repurchased 227,000 shares of common stock on the open market at a total cost of \$2.2 million. In Fiscal 2008, the Company repurchased 486,603 shares on the open market at a total cost of \$4.2 million. On July 12, 2007 the Company entered into a written trading plan under Rule 10b5-1 of the Exchange Act as part of the existing share repurchase program. As of October 19, 2007, the maximum dollar value of shares permitted to be purchased pursuant to the 10b5-1 plan had been purchased. The Company repurchased 363,800 shares on the open market during the first quarter of fiscal 2009 ended May 31, 2008 at a total cost of \$2.7 million. Of the one million share repurchase authorized in February 2006, all shares had been repurchased as of April 2008 at a total cost of \$8.6 million.
On January 7, 2008, our Board of Directors authorized the repurchase of up to one million additional shares of common stock, or approximately 7% of the shares outstanding at that time. The shares may be repurchased from time-to-time on the open market, subject to market conditions and other factors, and generally will be funded with

internally generated cash. This authorization was in addition to the shares that were remaining to be purchased under the February 2006 authorization. The Company repurchased 286,397 shares in the first quarter of fiscal 2009 to complete the one million shares authorized under the February 2006 authorization. The Company had repurchased 77,403 shares under the January 2008 authorization as of May 31, 2008.

		Cost of Shares	
		Purchased	
	Shares	(in thousands)	Average Price per Share
Treasury Stock as of February 29, 2008	4,902,251	\$ 52,978	\$ 10.81
Repurchases During the Three Months Ended May 31, 2008	363,800	2,706	7.44
Treasury Stock as of May 31, 2008	5,266,051	\$ 55,684	\$ 10.57

- (5) **Short-Term Investments.** The Company accounts for its short-term investments in accordance with Statement of Financial Accounting Standards No. 115, Accounting for Certain Investments in Debt and Equity Securities. In September 2007, the Company invested \$6.0 million in Auction-Rate Preferred Shares (ARS) from three different closed-end Nuveen funds. These investments are in the preferred shares of large diversified, highly-rated closed-end funds whose common shares are actively traded. The total value of assets of these funds is between two and three times the total value of the outstanding preferred shares in which we are invested. From September 2007 to mid-February 2008, the fund auctions occurred on a weekly basis and the Company exercised its right to either sell the shares at auction, or hold the shares and accept the new rate established by the auction. In mid-February 2008, the auctions started to fail as a result of the supply significantly exceeding demand for these investments, given the conditions in the overall economy and credit markets. The shares bear a higher rate of interest when auctions fail. The rate is equal to 150% of current AA commercial paper rates. Because of the shares having a preference over common shares and of the highly rated and diversified underlying assets, the Company believes that it will be able to liquidate these investments at par by the end of the fiscal year. The fund managers have announced and commenced providing substantial redemption to certain funds in which we are invested. We liquidated \$0.4 million in April 2008 at par value, \$2.4 million more in May 2008 at par value and \$0.5 million in June 2008 at par value. The Company has evaluated these assets for potential impairment related to the lack of liquidity and recorded a temporary impairment for \$0.1 million in the fourth quarter of fiscal 2008 with a charge to Other Comprehensive Income and a reduction in the carrying value of \$0.1 million for funds we expect to be redeemed later. There has been no change in the fair value of these securities as of May 31, 2008. Although we cannot be certain of a return of liquidity to these markets, we expect that these investments will be fully liquidated by the end of fiscal 2009, and they are therefore classified as short-term investments on our condensed consolidated balance sheet (unaudited).

The Company owns 28,404 shares of Manulife Financial Corporation. These shares are treated as available-for-sale equity securities. The Company's cost basis in this investment is \$0.2 million. The fair value of these securities was \$1.1 million as of May 31, 2008 and February 29, 2008.

As of May 31, 2008 and February 29, 2008 the Company held short term investments of \$4.1 million and \$6.9 million, respectively, which are auction rate preferred shares and shares of Manulife Financial Corporation stock. All income generated from these short-term investments is classified as other income.

(6) **Fair Value Measurements.** On March 1, 2008, the Company adopted SFAS No. 157, Fair Value Measurements (SFAS No. 157), for our financial assets and liabilities. This statement provides a framework for measuring fair value and requires expanded disclosures regarding fair value measurements. SFAS No. 157 defines fair value 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, which for the first quarter of fiscal 2009 is May 31, 2008. The fair-value hierarchy established in SFAS No. 157 prioritizes the inputs used in valuation techniques into three levels as follows:

Level 1 Observable inputs quoted prices in active markets for identical assets and liabilities;

Level 2 Observable inputs other than the quoted prices in active markets for identical assets and liabilities-such as quoted prices for similar instruments, quoted prices for identical or similar instruments in inactive markets, or other inputs that are observable or can be corroborated by observable market data;

Level 3 Unobservable inputs includes amounts derived from valuation models where one or more significant inputs are unobservable and require us to develop relevant assumptions.

The following table summarizes the financial assets measured at fair value on a recurring basis as of the measurement date, May 31, 2008, and the basis for that measurement, by level within the fair value hierarchy:

(in thousands)	Balance as of May 31, 2008	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Financial assets				
Equity Securities	\$ 4,132	\$ 1,098	\$ 3,034	

(7) **Comprehensive Loss**

(in thousands)

	Three Months Ended	
	May 31,	
	2008	2007
Net Loss	\$ (1,572)	\$ (545)
Other Comprehensive Income (Loss):		
Gain (Loss) on Marketable Securities, Net of Tax of \$0 and \$42, Respectively	(1)	66
Pension/Postretirement SFAS 158 Adjustments, Net of Benefit for Income Taxes of \$44, and \$0, Respectively	70	1
Foreign Currency Translation Adjustments	(50)	(175)
Comprehensive Loss	\$ (1,553)	\$ (653)