

KRONOS WORLDWIDE INC
Form 10-Q
November 06, 2013

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 quarter ended September 30, 2013

Commission file number 1-31763

KRONOS WORLDWIDE, INC.

(Exact name of Registrant as specified in its charter)

DELAWARE 76-0294959
(State or other jurisdiction (IRS Employer

of incorporation or organization) Identification No.)

5430 LBJ Freeway, Suite 1700

Dallas, Texas 75240-2697

(Address of principal executive offices)

Registrant's telephone number, including area code: (972) 233-1700

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 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 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 (as defined in Rule 12b-2 of the Securities Exchange Act of 1934). 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 Act). Yes No

Number of shares of the Registrant's common stock outstanding on October 31, 2013: 115,864,598.

KRONOS WORLDWIDE, INC. AND SUBSIDIARIES

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KRONOS WORLDWIDE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(In millions)

	December 31, 2012	September 30, 2013 (unaudited)
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 282.7	\$ 59.8
Restricted cash	2.7	1.9
Accounts and other receivables	285.8	336.9
Inventories	638.3	393.4
Prepaid expenses and other	9.8	12.9
Deferred income taxes	4.1	16.6
Total current assets	1,223.4	821.5
Other assets:		
Investment in TiO ₂ manufacturing joint venture	109.9	105.9
Marketable securities	21.6	34.5
Deferred income taxes	120.5	162.9
Other	29.1	25.0
Total other assets	281.1	328.3
Property and equipment:		
Land	45.2	45.4
Buildings	238.9	239.7
Equipment	1,082.9	1,092.1
Mining properties	131.3	128.5
Construction in progress	37.3	57.8
	1,535.6	1,563.5
Less accumulated depreciation and amortization	1,013.1	1,039.5
Net property and equipment	522.5	524.0
Total assets	\$ 2,027.0	\$ 1,673.8

KRONOS WORLDWIDE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS (CONTINUED)

(In millions)

	December 31, 2012	September 30, 2013 (unaudited)
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Current maturities of long-term debt	\$ 21.2	\$ 20.7
Accounts payable and accrued liabilities	273.2	265.5
Income taxes	23.1	.2
Deferred income taxes	10.9	11.0
Total current liabilities	328.4	297.4
Noncurrent liabilities:		
Long-term debt	378.9	203.3
Deferred income taxes	24.0	23.2
Accrued pension cost	189.2	184.3
Accrued postretirement benefit cost	14.1	14.1
Other	30.3	31.0
Total noncurrent liabilities	636.5	455.9
Stockholders equity:		
Common stock	1.2	1.2
Additional paid-in capital	1,399.1	1,398.5
Retained deficit	(141.1)	(298.2)
Accumulated other comprehensive loss	(197.1)	(181.0)
Total stockholders equity	1,062.1	920.5
Total liabilities and stockholders equity	\$ 2,027.0	\$ 1,673.8

Commitments and contingencies (Notes 8 and 12)

See accompanying Notes to Condensed Consolidated Financial Statements.

KRONOS WORLDWIDE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In millions, except per share data)

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2012	2013	2012	2013
	(unaudited)			
Net sales	\$ 472.9	\$ 419.1	\$ 1,579.5	\$ 1,363.8
Cost of sales	386.9	371.9	1,068.7	1,303.1
Gross margin	86.0	47.2	510.8	60.7
Selling, general and administrative expense	43.3	44.7	139.2	143.4
Currency transaction losses, net	(1.0)	(.3)	(.5)	(1.4)
Other operating expense, net	(3.2)	(39.2)	(12.6)	(47.5)
Income (loss) from operations	38.5	(37.0)	358.5	(131.6)
Other income (expense):				
Interest and dividend income	2.3	.3	6.6	.9
Loss on prepayment of debt		(2.3)	(7.2)	(8.9)
Interest expense	(7.0)	(4.5)	(20.0)	(16.6)
Income (loss) before income taxes	33.8	(43.5)	337.9	(156.2)
Income tax expense (benefit)	(1.4)	(13.6)	101.3	(51.3)
Net income (loss)	\$ 35.2	\$ (29.9)	\$ 236.6	\$ (104.9)
Net income (loss) per basic and diluted share	\$.30	\$ (.26)	\$ 2.04	\$ (.91)
Cash dividends per share	\$.15	\$.15	\$.45	\$.45
Weighted-average shares used in the calculation of net income (loss) per share	115.9	115.9	115.9	115.9

See accompanying Notes to Condensed Consolidated Financial Statements.

KRONOS WORLDWIDE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In millions)

	Three months ended September 30,		Nine months ended September 30,	
	2012	2013	2012	2013
	(unaudited)			
Net income (loss)	\$ 35.2	\$ (29.9)	\$ 236.6	\$ (104.9)
Other comprehensive income (loss), net of tax:				
Marketable securities adjustment	4.0	8.2	(13.9)	9.4
Currency translation adjustment	38.1	21.0	15.6	(.6)
Pension plans	1.7	2.4	5.2	7.4
OPEB plans			(.1)	(.1)
Total other comprehensive income	43.8	31.6	6.8	16.1
Comprehensive income (loss)	\$ 79.0	\$ 1.7	\$ 243.4	\$ (88.8)

See accompanying Notes to Condensed Consolidated Financial Statements.

KRONOS WORLDWIDE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY

Nine months ended September 30, 2013

(In millions)

	Common stock	Additional paid-in capital	Retained deficit	Accumulated other comprehensive loss (unaudited)	Treasury stock	Total stockholders equity
Balance at December 31, 2012	\$ 1.2	\$ 1,399.1	\$ (141.1)	\$ (197.1)	\$	\$ 1,062.1
Net loss			(104.9)			(104.9)
Other comprehensive income, net				16.1		16.1
Issuance of common stock		.1				.1
Dividends paid			(52.2)			(52.2)
Treasury stock acquired					(.7)	(.7)
Treasury stock retired		(.7)			.7	
Balance at September 30, 2013	\$ 1.2	\$ 1,398.5	\$ (298.2)	\$ (181.0)	\$	\$ 920.5

See accompanying Notes to Condensed Consolidated Financial Statements.

KRONOS WORLDWIDE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In millions)

	Nine months ended September 30, 2012 2013 (unaudited)	
Cash flows from operating activities:		
Net income (loss)	\$ 236.6	\$ (104.9)
Depreciation and amortization	35.4	37.6
Deferred income taxes	25.0	(62.1)
Loss on prepayment of debt, net	7.2	8.9
Call premium and interest paid on Senior Notes redeemed	(6.2)	
Benefit plan expense greater than cash funding:		
Defined benefit pension plans	.2	2.3
Other postretirement benefits	.2	.2
Distributions from (contributions to) TiO ₂ manufacturing joint venture, net	(30.1)	4.0
Other, net	.7	5.1
Change in assets and liabilities:		
Accounts and other receivables	(49.3)	(37.3)
Inventories	(158.2)	242.9
Prepaid expenses	(5.4)	(3.0)
Accounts payable and accrued liabilities	(46.8)	16.0
Income taxes	(5.3)	(8.8)
Accounts with affiliates	51.1	(40.7)
Other, net	2.4	.6
Net cash provided by operating activities	57.5	60.8
Cash flows from investing activities:		
Capital expenditures	(45.5)	(49.9)
Change in restricted cash equivalents, net	(1.6)	.6
Loans to Valhi:		
Loans	(95.3)	
Collections	63.8	
Proceeds from sale of marketable securities mutual funds	21.1	
Other, net		(.1)
Net cash used in investing activities	(57.5)	(49.4)
Cash flows from financing activities:		
Indebtedness:		
Borrowings	501.4	294.8
Principal payments	(414.9)	(476.5)
Dividends paid	(52.2)	(52.2)
Treasury stock acquired		(.7)
Other, net	(7.1)	
Net cash provided by (used in) financing activities	27.2	(234.6)

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Cash and cash equivalents net change from:		
Operating, investing and financing activities	27.2	(223.2)
Currency translation	1.2	.3
Balance at beginning of period	82.5	282.7
Balance at end of period	\$ 110.9	\$ 59.8
Supplemental disclosures:		
Cash paid for:		
Interest (including call premium paid)	\$ 28.9	\$ 15.6
Income taxes	84.6	33.6
Accrual for capital expenditures	4.5	3.7

See accompanying Notes to Condensed Consolidated Financial Statements.

KRONOS WORLDWIDE, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2013

(unaudited)

Note 1 Organization and basis of presentation:

Organization We are a majority-owned subsidiary of Valhi, Inc. (NYSE: VHI). At September 30, 2013, Valhi held approximately 50% of our outstanding common stock and NL Industries, Inc. (NYSE: NL) held an additional 30% of our common stock. Valhi owns approximately 83% of NL's outstanding common stock. Approximately 94% of Valhi's outstanding common stock is held by Contran Corporation and its subsidiaries. Substantially all of Contran's outstanding voting stock is held by trusts established for the benefit of certain children and grandchildren of Harold C. Simmons (for which Mr. Simmons is the sole trustee), or is held directly by Mr. Simmons or other persons or entities related to Mr. Simmons. Consequently, Mr. Simmons may be deemed to control Contran, Valhi and us.

Basis of presentation The unaudited Condensed Consolidated Financial Statements contained in this Quarterly Report have been prepared on the same basis as the audited Consolidated Financial Statements in our Annual Report on Form 10-K for the year ended December 31, 2012 that we filed with the Securities and Exchange Commission (SEC) on March 12, 2013 (2012 Annual Report). In our opinion, we have made all necessary adjustments (which include only normal recurring adjustments) in order to state fairly, in all material respects, our consolidated financial position, results of operations and cash flows as of the dates and for the periods presented. We have condensed the Consolidated Balance Sheet and Statement of Stockholders' Equity at December 31, 2012 contained in this Quarterly Report as compared to our audited Consolidated Financial Statements at that date, and we have omitted certain information and footnote disclosures (including those related to the Consolidated Balance Sheet at December 31, 2012) normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). Our results of operations for the interim periods ended September 30, 2013 may not be indicative of our operating results for the full year. The Condensed Consolidated Financial Statements contained in this Quarterly Report should be read in conjunction with our 2012 Consolidated Financial Statements contained in our 2012 Annual Report.

Unless otherwise indicated, references in this report to we, us or our refer to Kronos Worldwide, Inc. and its subsidiaries (NYSE: KRO) taken as a whole.

Note 2 Accounts and other receivables:

December 31, September 30,
2012 2013
(In millions)

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Trade receivables	\$ 229.7	\$ 276.5
Recoverable VAT and other receivables	38.9	37.5
Receivable from affiliate Louisiana Pigment Company, L.P.		18.1
Refundable income taxes	18.3	5.9
Allowance for doubtful accounts	(1.1)	(1.1)
Total	\$ 285.8	\$ 336.9

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Note 3 Inventories, net:

	December 31, 2012	September 30, 2013
	(In millions)	
Raw materials	\$ 151.5	\$ 69.3
Work in process	27.3	18.1
Finished products	394.8	237.0
Supplies	64.7	69.0
Total	\$ 638.3	\$ 393.4

Note 4 Marketable securities:

Our marketable securities consist of investments in the publicly-traded shares of related parties: Valhi, NL and CompX International Inc. NL owns a majority of CompX's outstanding common stock. All of our marketable securities are accounted for as available-for-sale securities, which are carried at fair value using quoted market prices in active markets for each marketable security, and represent a Level 1 input within the fair value hierarchy. See Note 13. Because we have classified all of our marketable securities as available-for-sale, any unrealized gains or losses on the securities are recognized through other comprehensive income, net of deferred income taxes.

Marketable security	Fair value measurement level	Market value	Cost basis	Unrealized gains
(In millions)				
As of December 31, 2012:				
Valhi common stock	1	\$ 21.5	\$ 15.3	\$ 6.2
NL and CompX common stocks	1	.1	.1	
Total		\$ 21.6	\$ 15.4	\$ 6.2
As of September 30, 2013:				
Valhi common stock	1	\$ 34.4	\$ 15.3	\$ 19.1
NL and CompX common stocks	1	.1	.1	
Total		\$ 34.5	\$ 15.4	\$ 19.1

At December 31, 2012 and September 30, 2013, we held approximately 1.7 million shares of Valhi's common stock with a quoted per share market price of \$12.50 and \$19.96, respectively. We also held a nominal number of shares of CompX and NL common stocks.

The Valhi, CompX and NL common stocks we own are subject to the restrictions on resale pursuant to certain provisions of SEC Rule 144. In addition, as a majority-owned subsidiary of Valhi we cannot vote our shares of Valhi

common stock under Delaware Corporation Law, but we do receive dividends from Valhi on these shares, when declared and paid.

Note 5 Other noncurrent assets:

	December 31, 2012	September 30, 2013
(In millions)		
Deferred financing costs, net	\$ 7.0	\$ 2.6
Restricted cash	7.5	7.2
Pension asset	5.1	5.8
Other	9.5	9.4
Total	\$ 29.1	\$ 25.0

Note 6 Accounts payable and accrued liabilities:

	December 31, 2012	September 30, 2013
(In millions)		
Accounts payable	\$ 161.3	\$ 118.7
Employee benefits	29.6	29.3
Accrued sales discounts and rebates	14.9	15.0
Accrued interest	.2	.1
Accrued legal settlement		35.0
Payable to affiliates:		
Income taxes, net Valhi	18.1	2.5
Louisiana Pigment Company, L.P.	23.5	19.5
Other	25.6	45.4
Total	\$ 273.2	\$ 265.5

The accrued legal settlement is discussed in Note 12.

Note 7 Long-term debt:

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	December 31, 2012	September 30, 2013
	(In millions)	
Term loan	\$ 384.5	\$
Note payable to Contran		175.0
Revolving European credit facility	13.2	
Revolving North American credit facility		46.2
Other	2.4	2.8
Total debt	400.1	224.0
Less current maturities	21.2	20.7
Total long-term debt	\$ 378.9	\$ 203.3

Term loan In February 2013, we voluntarily prepaid an aggregate \$290 million principal amount of our term loan. We recognized a non-cash pre-tax interest charge of \$6.6 million in the first quarter of 2013 related to this prepayment consisting of the write-off of the unamortized original issue discount costs and deferred financing costs associated with such prepayment. Funds for such prepayment were provided by \$100 million of our cash on hand as well as borrowings of \$190 million under a new loan from Contran as described below. In July 2013, we voluntarily prepaid the remaining \$100 million principal amount outstanding under our term loan, using \$50 million of our cash on hand and borrowings of \$50 million under our revolving North American credit facility. We recognized a non-cash pre-tax interest charge of \$2.3 million in the third quarter of 2013 related to this prepayment consisting of

the write-off of the unamortized original issue discount costs and deferred financing costs associated with such prepayment. The average interest rate on the term loan for the year-to-date period ended July 30, 2013 (the payoff date) was 6.8%.

Note payable to Contran As discussed above, in February 2013 we entered into a promissory note with Contran that allows us to borrow up to \$290 million. This new loan from Contran contains terms and conditions similar to the terms and conditions of the term loan, except that the loan from Contran is unsecured and contains no financial maintenance covenant. The independent members of our board of directors approved the terms and conditions of the loan from Contran. The note requires quarterly principal payments of \$5.0 million which commenced in March 2013, with any remaining outstanding principal due by June 2018. Voluntary principal prepayments are permitted at any time without penalty. The note bears interest at LIBOR (with LIBOR no less than 1%) plus 5.125%, or the base rate (as defined in the agreement) plus 4.125%. We are required to use the base rate method until such time as both (1) the term loan discussed above has been fully repaid and (2) the European credit facility has been amended on terms satisfactory to Contran, at which time we would have the option to use either the base rate or LIBOR rate methods. The average interest rate on these borrowings as of and for the period from issuance to September 30, 2013 was 7.375%.

Revolving European credit facility During the first nine months of 2013, we borrowed 10 million (\$12.8 million when borrowed) and repaid the entire outstanding balance of 20 million (\$26.5 million when repaid) in August under our European credit facility. The average interest rate on these borrowings for the year-to-date period ended August 31, 2013 when paid off was 2.02%. At September 30, 2013, there were no outstanding borrowings under this facility.

Our European credit facility requires the maintenance of certain financial ratios. At September 30, 2013, based on the current earnings before income tax, interest, depreciation and amortization expense of the borrowers, we would not have met the financial test if we had any net debt outstanding under this facility, and accordingly our effective available borrowing under this facility at September 30, 2013 is approximately \$32.4 million, the aggregate amount of cash held by the borrowers, net of the borrowers' other outstanding indebtedness. We are in discussions with the lender to amend the facility to modify the covenant. However, we do not currently anticipate the need to draw on this facility for the foreseeable future.

Revolving North American credit facility During the first nine months of 2013, we borrowed \$90.3 million and repaid an aggregate \$44.1 million. The average interest rate on these borrowings as of and for the period from borrowing to September 30, 2013 was 2.63% and 2.46%, respectively. At September 30, 2013 we had approximately \$56.6 million available for borrowing under this revolving facility.

Canada At September 30, 2013, an aggregate of Cdn. \$7.5 million letters of credit were outstanding under our Canadian subsidiary's loan agreement with the Bank of Montreal which exists solely for the issuance of up to Cdn. \$10.0 million in letters of credit.

In January 2013, we borrowed Cdn. \$1.8 million (USD \$1.8 million) under our Canadian subsidiary's agreement with an economic development agency of the Province of Quebec, Canada which was recorded net of Cdn. \$.5 million (USD \$.5 million) imputed interest.

Restrictions and other Our European credit facility described above requires the borrowers to maintain minimum levels of equity, requires the maintenance of certain financial ratios, limits dividends and additional indebtedness and contains other provisions and restrictive covenants customary in lending transactions of this type. Our North American revolving credit facility and note payable to Contran also contain restrictive covenants. At September 30, 2013, there were no restrictions on our ability to pay dividends.

We are in compliance with all of our debt covenants at September 30, 2013.

Note 8 Income taxes:

	Three months ended		Nine months ended	
	September 30, 2012	2013	September 30, 2012	2013
	(In millions)			
Expected tax expense (benefit), at U.S. Federal statutory income tax rate of 35%	\$ 11.9	\$ (15.3)	\$ 118.3	\$ (54.7)
Non-U.S. tax rates	(.8)	.7	(12.5)	3.2
Incremental tax (benefit) on earnings (losses) of non-U.S. companies	(12.8)	1.3	(7.1)	(3.4)
U.S. State income taxes and other, net	.3	(.3)	2.6	3.6
Total	\$ (1.4)	\$ (13.6)	\$ 101.3	\$ (51.3)
Comprehensive provision for income taxes (benefit) allocable to:				
Net income (loss)	\$ (1.4)	\$ (13.6)	\$ 101.3	\$ (51.3)
Other comprehensive income (loss):				
Marketable securities	2.1	3.8	(7.9)	4.5
Currency translation	4.4	4.1	2.7	2.8
Pension plans	.7	1.1	2.2	3.3
OPEB plans			(.1)	(.1)
Total	\$ 5.8	\$ (4.6)	\$ 98.2	\$ (40.8)

Our income tax benefit in the third quarter of 2012 includes an incremental tax benefit of \$11.1 million as we determined in the third quarter 2012 that due to global changes in our business, we would not remit certain dividends from our non-U.S. jurisdictions. As a result, certain tax attributes were available for carryback to offset prior year tax expense.

In the third quarter of 2012, France enacted certain changes in their income tax laws, including a 3% nondeductible surtax on all dividend distributions which tax is assessed at the time of the distribution against the company making such distribution. Consequently, our French subsidiary will be required to pay an additional 3% tax on all future dividend distributions. Our undistributed earnings in France are deemed to be permanently reinvested and such tax will be recognized as part of our income tax expense in the period during which the dividend is declared and will be remitted to the French government in accordance with the applicable tax law. During the third quarter of 2012, our French subsidiary distributed a \$1.8 million dividend. Distributions from our French subsidiary in 2013 are nil. At September 30, 2013, our French subsidiary has undistributed earnings of approximately \$10.9 million that, if distributed, would be subject to the 3% surtax.

Tax authorities are examining certain of our U.S. and non-U.S. tax returns and have or may propose tax deficiencies, including penalties and interest. Because of the inherent uncertainties involved in settlement initiatives and court and tax proceedings, we cannot guarantee that these matters will be resolved in our favor, and therefore our potential exposure, if any, is also uncertain. In 2011 and 2012, we received notices of re-assessment from the Canadian federal and provincial tax authorities related to the years 2002 through 2004. We object to the re-assessments and believe the position is without merit. Accordingly, we are appealing the re-assessments and in connection with such appeal we were required to post letters of credit aggregating Cdn. \$7.5 million (see Note 7). If the full amount of the proposed adjustment were ultimately to be assessed against us, the cash tax liability would be approximately \$15.7 million. We

believe we have adequate accruals for additional taxes and related interest expense which could ultimately result from tax examinations. We believe the ultimate disposition of tax examinations should not have a material adverse effect on our consolidated financial position, results of operations or liquidity. We currently estimate that our unrecognized tax benefits may change by \$3 million during the next twelve months related to certain adjustments to our prior year returns.

Note 9 Employee benefit plans:

Defined benefit plans The components of net periodic defined benefit pension cost are presented in the table below.

	Three months ended		Nine months ended	
	September 30, 2012	September 30, 2013	September 30, 2012	September 30, 2013
	(In millions)			
Service cost	\$ 2.5	\$ 3.2	\$ 7.7	\$ 9.7
Interest cost	5.6	5.4	17.2	16.2
Expected return on plan assets	(4.5)	(4.9)	(13.7)	(14.9)
Amortization of prior service cost	.4	.4	1.2	1.2
Amortization of net transition obligations	.1	.1	.3	.3
Recognized actuarial losses	1.9	3.1	5.9	9.3
Total	\$ 6.0	\$ 7.3	\$ 18.6	\$ 21.8

Postretirement benefits The components of net periodic postretirement benefits other than pension (OPEB) cost are presented in the table below.

	Three months ended		Nine months ended	
	September 30, 2012	September 30, 2013	September 30, 2012	September 30, 2013
	(In millions)			
Service cost	\$.1	\$.1	\$.2	\$.3
Interest cost	.1	.2	.4	.4
Amortization of prior service credit	(.2)	(.2)	(.5)	(.5)
Recognized actuarial loss	.1	.1	.3	.3
Total	\$.1	\$.2	\$.4	\$.5

Contributions We expect our 2013 contributions for our pension and other postretirement plans to be approximately \$28 million.

Note 10 Other noncurrent liabilities:

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	December 31, 2012	September 30, 2013
	(In millions)	
Reserve for uncertain tax positions	\$ 13.4	\$ 14.4
Employee benefits	11.3	10.9
Other	5.6	5.7
Total	\$ 30.3	\$ 31.0

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Note 11 Accumulated other comprehensive loss:

Changes in accumulated other comprehensive loss for the three and nine months ended September 30, 2012 and 2013 are presented in the table below.

	Three months ended September 30,		Nine months ended September 30,	
	2012	2013	2012	2013
	(In millions)			
Accumulated other comprehensive loss, net of tax:				
Marketable securities:				
Balance at beginning of period	\$ (12.8)	\$ 5.4	\$ 5.1	\$ 4.2
Other comprehensive income (loss) unrealized gains (losses) arising during the year	4.0	8.2	(13.9)	9.4
Balance at end of period	\$ (8.8)	\$ 13.6	\$ (8.8)	\$ 13.6
Currency translation:				
Balance at beginning of period	\$ (114.3)	\$ (85.1)	\$ (91.8)	\$ (63.5)
Other comprehensive income (loss)	38.1	21.0	15.6	(.6)
Balance at end of period	\$ (76.2)	\$ (64.1)	\$ (76.2)	\$ (64.1)
Defined benefit pension plans:				
Balance at beginning of period	\$ (95.7)	\$ (132.3)	\$ (99.2)	\$ (137.3)
Other comprehensive income amortization of prior service cost and net losses included in net periodic pension cost	1.7	2.4	5.2	7.4
Balance at end of period	\$ (94.0)	\$ (129.9)	\$ (94.0)	\$ (129.9)
OPEB plans:				
Balance at beginning of period	\$	\$ (.6)	\$.1	\$ (.5)
Other comprehensive loss amortization of prior service credit and net losses included in net periodic OPEB cost			(.1)	(.1)
Balance at end of period	\$	\$ (.6)	\$	\$ (.6)
Total accumulated other comprehensive loss:				
Balance at beginning of period	\$ (222.8)	\$ (212.6)	\$ (185.8)	\$ (197.1)
Other comprehensive income	43.8	31.6	6.8	16.1
Balance at end of period	\$ (179.0)	\$ (181.0)	\$ (179.0)	\$ (181.0)

See Note 9 for amounts related to our defined benefit pension plans and OPEB plans.

Note 12 Commitments and contingencies:

From time-to-time, we are involved in various environmental, contractual, product liability, patent (or intellectual property), employment and other claims and disputes incidental to our operations. In certain cases, we have insurance coverage for these items. We currently believe the disposition of all claims and disputes, individually or in the aggregate, should not have a material adverse effect on our consolidated financial position, results of operations or liquidity beyond the accruals we have already provided.

In March 2010, we were served with two complaints which were subsequently consolidated as Haley Paint et al. v. E.I. Du Pont de Nemours and Company, et al. (United States District Court, for the District of Maryland, Case No. 1:10-cv-00318-RDB). A third plaintiff intervened into the case in July 2011. The defendants included us, E.I. Du Pont de Nemours & Company, Huntsman International LLC, Millennium Inorganic Chemicals, Inc. and the National Titanium Dioxide Company Limited (d/b/a Cristal). Plaintiffs sought to represent a class consisting of all persons and entities that purchased titanium dioxide in the United States directly from one or more of the defendants on or after March 1, 2002. The complaint alleged that the defendants conspired and combined to fix, raise, maintain, and stabilize the price at which titanium dioxide was sold in the United States and engaged in other anticompetitive conduct. In May 2010, defendants filed a motion to dismiss, which plaintiffs opposed. In March 2011, the court denied the motion to dismiss. In February 2012, the plaintiffs submitted their motion for class certification, which defendants opposed. In August 2012, the court granted the plaintiffs' motion for class certification and trial was set for September 2013. On September 10, 2013, and following the agreement by the three other defendants in the third quarter of 2013 to enter into settlement agreements with the class plaintiffs, we also entered into a settlement agreement with the class plaintiffs, without admitting any fault

or wrongdoing, and agreed to pay an aggregate of \$35 million (payable in two installments at specified times, expected to occur by mid-2014). Following the service of the Class Action Fairness Notice and the Order of Final Approval from the court, we, and the other defendants, will be dismissed with prejudice from this matter. Other operating expense in the third quarter of 2013 includes a \$35 million charge related to this settlement. See also Note 6.

In March 2013, we were served with the complaint, Los Gatos Mercantile, Inc. d/b/a Los Gatos Ace Hardware, et al v. E.I. Du Pont de Nemours and Company, et al. (United States District Court, for the Northern District of California, Case No. 3:13-cv-01180-SI). The defendants include us, E.I. Du Pont de Nemours & Company, Huntsman International LLC and Millennium Inorganic Chemicals, Inc. Plaintiffs seek to represent a class consisting of indirect purchasers of titanium dioxide in the states of Arizona, Arkansas, California, the District of Columbia, Florida, Hawaii, Illinois, Iowa, Kansas, Maine, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Hampshire, New Mexico, New York, North Carolina, North Dakota, Oregon, South Carolina, South Dakota, Tennessee, Utah, Vermont, West Virginia and Wisconsin that indirectly purchased titanium dioxide from one or more of the defendants on or after March 1, 2002. The complaint alleges that the defendants conspired and combined to fix, raise, maintain, and stabilize the price at which titanium dioxide was sold in the United States and engaged in other anticompetitive conduct. This matter had been stayed by the court pending a resolution in the Haley Paint Matter. The case is now proceeding in the trial court. We believe the action is without merit, will deny all allegations of wrongdoing and liability and intend to defend against the action vigorously.

Note 13 Financial instruments:

The following table summarizes the valuation of our financial instruments recorded on a fair value basis as of December 31, 2012 and September 30, 2013:

	Total	Fair Value Measurements		
		Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(In millions)				
Asset (liability)				
December 31, 2012				
Currency forward contracts	\$ 1.8	\$ 1.8	\$	\$
Noncurrent marketable securities (See Note 4)	21.6	21.6		
September 30, 2013				
Currency forward contracts	\$ (.5)	\$ (.5)	\$	\$
Noncurrent marketable securities (See Note 4)	34.5	34.5		

Certain of our sales generated by our non-U.S. operations are denominated in U.S. dollars. We periodically use currency forward contracts to manage a very nominal portion of currency exchange rate risk associated with trade receivables denominated in a currency other than the holder's functional currency or similar exchange rate risk associated with future sales. We have not entered into these contracts for trading or speculative purposes in the past,

nor do we currently anticipate entering into such contracts for trading or speculative purposes in the future.

Derivatives used to hedge forecasted transactions and specific cash flows associated with financial assets and liabilities denominated in currencies other than the U.S. dollar and which meet the criteria for hedge accounting are designated as cash flow hedges. Consequently, the effective portion of gains and losses is deferred as a component of accumulated other comprehensive income and is recognized in earnings at the time the hedged item affects earnings.

Contracts that do not meet the criteria for hedge accounting are marked-to-market at each balance sheet date with any resulting gain or loss recognized in income currently as part of net currency transactions. The fair value of the currency forward contracts is determined using Level 1 inputs based on the currency spot forward rates quoted by banks or currency dealers.

At September 30, 2013, we had currency forward contracts to exchange:

·an aggregate of \$45.0 million for an equivalent value of Canadian dollars at an exchange rate ranging from Cdn. \$1.02 to Cdn. \$1.06 per U.S. dollar. These contracts with Wells Fargo Bank, N.A. mature from October 2013 through December 2014 at a rate of \$3.0 million per month, subject to early redemption provisions at our option;

·an aggregate \$25.0 million for an equivalent value of Norwegian kroner at exchange rates ranging from kroner 5.84 to kroner 6.14 per U.S. dollar. These contracts with DnB Nor Bank ASA mature at a rate of \$5.0 million per month in certain months from October 2013 through April 2014; and

·an aggregate 16.0 million for an equivalent value of Norwegian kroner at exchange rates ranging from kroner 7.55 to kroner 8.07 per euro. These contracts with DnB Nor Bank ASA mature at a rate ranging from 2.0 million to 5.0 million per month in certain months from October 2013 through April 2014.

The estimated fair value of our currency forward contracts at September 30, 2013 was a net liability of \$.5 million, of which \$.8 million is recognized as part of accounts and other receivables and \$1.3 million is recognized as part of accounts payable and accrued liabilities, in our Condensed Consolidated Balance Sheets. There is also a corresponding \$.5 million currency transaction loss recognized in our Condensed Consolidated Statement of Operations. We are not currently using hedge accounting for our outstanding currency forward contracts at September 30, 2013, and we did not use hedge accounting for any of such contracts we previously held in 2012.

The following table presents the financial instruments that are not carried at fair value but which require fair value disclosure as of December 31, 2012 and September 30, 2013.

	December 31, 2012		September 30, 2013	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	(In millions)			
Cash, cash equivalents and restricted cash	\$ 292.9	\$ 292.9	\$ 68.9	\$ 68.9
Notes payable and long-term debt:				
Variable rate:				
Term loan	384.5	396.8		
Note payable to Contran			175.0	175.0
European credit facility	13.2	13.2		
North American credit facility			46.2	46.2
Common stockholders' equity	1,062.1	2,260.2	920.5	1,794.7

At December 31, 2012, the estimated market price of our term loan was \$1,017.5 per \$1,000 principal amount. The fair value of our term loan is based on quoted market prices; however, these quoted market prices represent Level 2 inputs because the markets in which the term loan trades were not active. The fair values of our note payable to Contran and our European credit facility represent Level 2 inputs, and are deemed to approximate book value. The fair value of our common stockholders' equity is based upon quoted market prices at each balance sheet date, which represent Level 1 inputs. Due to their near-term maturities, the carrying amounts of accounts receivable and accounts payable are considered equivalent to fair value.

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

RESULTS OF OPERATIONS:

Business overview

We are a leading global producer and marketer of value-added titanium dioxide pigments (TiO₂). TiO₂ is used for a variety of manufacturing applications, including coatings, plastics, paper and other industrial products. For the nine months ended September 30, 2013, approximately one-half of our sales volumes were into European markets. Our production facilities are located in Europe and North America.

We consider TiO₂ to be a "quality of life" product, with demand affected by gross domestic product, or GDP, and overall economic conditions in our markets located in various regions of the world. Over the long-term, we expect demand for TiO₂ will grow by 2% to 3% per year, consistent with our expectations for the long-term growth in GDP. However, even if we and our competitors maintain consistent shares of the worldwide market, demand for TiO₂ in any interim or annual period may not change in the same proportion as the change in GDP, in part due to relative changes in the TiO₂ inventory levels of our customers. We believe that our customers' inventory levels are influenced in part by their expectations for future changes in market TiO₂ selling prices as well as their expectations for future availability of product. Although certain of our TiO₂ grades are considered specialty pigments, the majority of our grades and substantially all of our production are considered commodity pigment products, with price and availability being the most significant competitive factors along with quality and customer service.

The factors having the most impact on our reported operating results are:

- our TiO₂ sales and production volumes,
- TiO₂ selling prices,
- currency exchange rates (particularly the exchange rate for the U.S. dollar relative to the euro, Norwegian krone and Canadian dollar) and
- manufacturing costs, particularly raw materials, maintenance and energy-related expenses.

Our key performance indicators are our TiO₂ average selling prices and our TiO₂ sales and production volumes. TiO₂ selling prices generally follow industry trends and prices will increase or decrease generally as a result of competitive market pressures.

Executive summary

We reported a net loss of \$29.9 million, or \$.26 per share, in the third quarter of 2013 as compared to net income of \$35.2 million, or \$.30 per share, in the third quarter of 2012. For the first nine months of 2013, we reported a net loss of \$104.9 million, or \$.91 per share, compared to net income of \$236.6 million, or \$2.04 per share, in the first nine months of 2012. We had a net loss in the third quarter of 2013 compared to net income in the third quarter of 2012 principally due to a loss from operations in 2013 resulting from lower average selling prices and a litigation settlement charge, partially offset by lower raw material costs and higher production volumes. We had a net loss in the first nine months of 2013 compared to net income in the first nine months of 2012 principally due to a loss from operations in 2013 resulting from the unfavorable effects of lower average selling prices and higher raw material costs in 2013 and the litigation settlement charge.

Our results in the first nine months of 2013 include a first quarter non-cash pre-tax charge of \$6.6 million (\$4.3 million, or \$.04 per share, net of income tax benefit) and a third quarter charge of \$2.3 million (\$1.5 million, or \$.01 per share, net of income tax benefit) related to the voluntary prepayment of \$290 million and \$100 million principal

amount, respectively, of our term loan, consisting of the write-off of original issue discount costs and deferred financing costs associated with such prepayments. Our results in the third quarter of 2013 also include a pre-tax litigation settlement of \$35 million (\$22.5 million, or \$.19 per share, net of income tax benefit). Our results in the first nine months of 2012 include an aggregate second quarter charge of \$7.2 million (\$4.7 million, or \$.04 per share, net of income tax benefit) associated with the June 2012 redemption of the remaining 279.2 million principal amount of our Senior Notes, consisting of the call premium paid, interest from the June 14, 2012 indenture discharge date to the July 20, 2012 redemption date and the write-off of unamortized deferred financing costs and original issue discount.

Forward-looking information

This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, as amended. Statements in this Quarterly Report on Form 10-Q that are not historical facts are forward-looking in nature and represent management's beliefs and assumptions based on currently available information. Statements in this report including, but not limited to, statements found in Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations, are forward-looking statements that represent our management's beliefs and assumptions based on currently available information. In some cases you can identify forward-looking statements by the use of words such as believes, intends, may, should, could, anticipates, expects or comparable terminology in discussions of strategies or trends. Although we believe the expectations reflected in forward-looking statements are reasonable, we do not know if these expectations will be correct. Such statements by their nature involve substantial risks and uncertainties that could significantly impact expected results. Actual future results could differ materially from those predicted. The factors that could cause our actual future results to differ materially from those described herein are the risks and uncertainties discussed in this Quarterly Report and those described from time to time in our other filings with the SEC including, but are not limited to, the following:

- Future supply and demand for our products

- The extent of the dependence of certain of our businesses on certain market sectors

- The cyclical nature of our business

- Customer and producer inventory levels

- Unexpected or earlier-than-expected industry capacity expansion

- Changes in raw material and other operating costs (such as ore and energy costs)

- Changes in the availability of raw materials (such as ore)

- General global economic and political conditions (such as changes in the level of gross domestic product in various regions of the world and the impact of such changes on demand for TiO₂)

- Competitive products and substitute products

- Customer and competitor strategies

- Potential consolidation of our competitors

- Potential consolidation of our customers

- The impact of pricing and production decisions

- Competitive technology positions

- The introduction of trade barriers

- Possible disruption of our business, or increases in our cost of doing business, resulting from terrorist activities or global conflicts

- Fluctuations in currency exchange rates (such as changes in the exchange rate between the U.S. dollar and each of the euro, the Norwegian krone and the Canadian dollar), or possible disruptions to our business resulting from potential instability resulting from uncertainties associated with the euro

- Operating interruptions (including, but not limited to, labor disputes, leaks, natural disasters, fires, explosions, unscheduled or unplanned downtime, transportation interruptions and cyber attacks)

- Our ability to renew or refinance credit facilities

- Our ability to maintain sufficient liquidity

- The ultimate outcome of income tax audits, tax settlement initiatives or other tax matters

- Our ability to utilize income tax attributes, the benefits of which have been recognized under the more-likely-than-not recognition criteria

·Environmental matters (such as those requiring compliance with emission and discharge standards for existing and new facilities)

·Government laws and regulations and possible changes therein

·The ultimate resolution of pending litigation

·Possible future litigation.

Should one or more of these risks materialize (or the consequences of such a development worsen), or should the underlying assumptions prove incorrect, actual results could differ materially from those forecasted or expected. We disclaim any intention or obligation to update or revise any forward-looking statement whether as a result of changes in information, future events or otherwise.

Results of operations

Quarter ended September 30, 2013 compared to the quarter ended September 30, 2012

	Three months ended September 30,			
	2012		2013	
	(Dollars in millions)			
Net sales	\$ 472.9	100%	\$ 419.1	100%
Cost of sales	386.9	82	371.9	89
Gross margin	86.0	18	47.2	11
Other operating expense, net	47.5	10	84.2	20
Income (loss) from operations	\$ 38.5	8%	\$ (37.0)	(9)%

%

	Change		
TiO ₂ operating statistics:			
Sales volumes*	116	121	4%
Production volumes*	98	113	15%
Percentage change in net sales:			
TiO ₂ product pricing			(18)%
TiO ₂ sales volumes			4
TiO ₂ product mix			1
Changes in currency exchange rates			2
Total			(11)%

*Thousands of metric tons

Current industry conditions In the second quarter of 2013, we announced price increases for our TiO₂ products in all of our markets, implementation of which began in June 2013. In the third quarter of 2013, we notified customers of additional price increases to be implemented beginning in October 2013. As a result, after about a year of decreasing selling prices within the TiO₂ industry, our selling prices have generally stabilized. Our average selling prices at the end of the third quarter of 2013 were 1% higher than at the end of the second quarter of 2013, and were 7% lower than at the end of 2012. Demand for TiO₂ products has generally been strong in 2013, primarily in European and export markets, as customers have generally depleted their inventories in response to general global economic uncertainty.

While we operated our production facilities at full practical capacity rates in the first quarter of 2012, we operated our facilities at reduced rates during the remainder of 2012 (approximately 86% of practical capacity in the second quarter, approximately 71% in the third quarter and approximately 80% in the fourth quarter) to align production levels and inventories to current and anticipated near-term customer demand levels. We continued to operate our production facilities at reduced capacity rates in the first nine months of 2013 (approximately 92% of practical capacity in the first quarter, approximately 90% in the second quarter and approximately 82% in the third quarter).

We experienced significantly higher costs for our raw materials such as third party feedstock ore and petroleum coke in 2012. We operate two ilmenite mines in Norway, the production from which provides all of the feedstock for our European sulfate process

facilities as well as third party ilmenite ore sales. Our cost of sales per metric ton of TiO₂ sold in the first half of 2013 was significantly higher than TiO₂ sold in the first half of 2012, as a substantial portion of the TiO₂ products we sold in the first quarter of 2012 (and a portion of the TiO₂ products we sold in the second quarter of 2012) was produced with lower-cost feedstock ore purchased in 2011, while a substantial portion of the TiO₂ products we sold in the first quarter of 2013 (and a portion of the TiO₂ products we sold in the second quarter of 2013) was produced with higher-cost feedstock ore purchased in 2012. We have seen some moderation in the cost of TiO₂ feedstock ore procured from third parties in 2013, but such reductions did not begin to be significantly reflected in our cost of sales until the third quarter of 2013. As expected, our cost of sales per metric ton of TiO₂ sold in the third quarter of 2013 was lower than the cost of sales per metric ton of TiO₂ sold in the third quarter of 2012, primarily due to the lower feedstock ore costs.

Net sales Net sales in the third quarter of 2013 decreased 11%, or \$53.8 million, compared to the third quarter of 2012 primarily due to the net effects of an 18% decrease in average TiO₂ selling prices (which decreased net sales by approximately \$85 million) and a 4% increase in sales volumes (which increased net sales by approximately \$19 million). TiO₂ selling prices will increase or decrease generally as a result of competitive market pressures, changes in the relative level of supply and demand as well as changes in raw material and other manufacturing costs.

Our sales volumes increased 4% in the third quarter of 2013 as compared to the third quarter of 2012 due to higher customer demand in European markets partially offset by lower sales in export and North American markets. In addition, we estimate the favorable effect of changes in currency exchange rates increased our net sales by approximately \$12 million as compared to the third quarter of 2012.

Cost of sales Cost of sales decreased \$15.0 million or 4% in the third quarter of 2013 compared to 2012 due to the net impact of lower raw material costs of approximately \$28 million (primarily feedstock ore), a 4% increase in sales volumes, a 15% increase in TiO₂ production volumes and currency fluctuations (primarily the euro). As expected, the cost of sales per metric ton of TiO₂ sold in the third quarter of 2013 was lower than the cost of sales per metric ton of TiO₂ sold in the third quarter of 2012 primarily due to the lower feedstock ore costs. In the third quarter of 2012 we operated our facilities at a reduced rate in an effort to align inventory levels with lower demand. The reduction in our TiO₂ production volumes during that time resulted in approximately \$25 million of unabsorbed fixed production costs which were charged directly to cost of sales. Cost of sales as a percentage of net sales increased to 89% in the third quarter of 2013 compared to 82% in the in the same period of 2012 primarily due to the net effects of lower average selling prices, lower raw materials costs and lower unabsorbed fixed costs, as discussed and quantified above.

Unionized employees in our Canadian TiO₂ production facility are covered by a collective bargaining agreement that expired June 15, 2013. The Canadian facility represents approximately 19% of our worldwide TiO₂ production capacity. The union employees represented by the Confederation des Syndicat National (CSN) rejected our revised global offer, and we declared a lockout of unionized employees upon the expiration of the existing contract. As of the date of this report, no agreement has been reached with the CSN and the unionized employees remain locked out. We are currently operating our Canadian plant at approximately 15% of the plant's capacity with non-union management employees, and have implemented a strategy to reduce the financial impact of operating the plant during the lockout. Since the lockout began, we have been able to fill customer orders with inventory on hand or through production from our other facilities, and we expect to similarly continue meeting customer demand for the foreseeable future. There is no assurance that we will be able to reach an agreement with the CSN on the terms of a new collective bargaining agreement, or reach an agreement on terms that will not have a material adverse effect on our results of operations.

Other operating expense, net Other operating expense in the third quarter of 2013 includes a \$35 million litigation settlement charge. See Note 12 to our Condensed Consolidated Financial Statements.

Gross margin and income (loss) from operations Income (loss) from operations decreased by \$75.5 million from income of \$38.5 million in the third quarter of 2012 to a loss of \$37.0 million in the third quarter of 2013. Income

(loss) from operations as a percentage of net sales decreased to (9)% in the third quarter of 2013 from 8% in the same period of 2012. This decrease was driven by the decline in gross margin, which decreased to 11% for the third quarter of 2013 compared to 18% for the third quarter of 2012, and by the 2013 litigation settlement charge discussed above.

As discussed and quantified above, our gross margin has decreased primarily due to the net effects of lower selling prices, lower manufacturing costs (primarily raw materials), higher sales volumes and higher production volumes.

Additionally, changes in currency exchange rates have positively affected our gross margin and income from operations. We estimate that changes in currency exchange rates increased income from operations by approximately \$1 million in the third quarter of 2013 as compared to the same period in 2012.

Other non-operating income (expense) We recognized an aggregate \$2.3 million pre-tax charge, consisting of the write-off of unamortized original issue discount costs and deferred financing costs, in the third quarter of 2013 related to the voluntary prepayment of the remaining \$100 million principal amount outstanding under our term loan. See Note 7 to our Condensed Consolidated Financial Statements.

Interest expense decreased \$2.5 million from \$7.0 million in the third quarter of 2012 to \$4.5 million in the third quarter of 2013 primarily due to lower average debt levels in 2013.

Interest and dividend income decreased \$2.0 million to \$.3 million in the third quarter of 2013 primarily due to lower balances available for investment, principally related to our loan to Valhi which was completely repaid in December 2012. Interest income on our loan to Valhi was \$1.8 million in the third quarter of 2012.

Income tax benefit We recognized an income tax benefit of \$13.6 million in the third quarter of 2013 compared to a benefit of \$1.4 million in the same period last year. This difference is due in part to our decreased earnings in 2013.

In addition, our income tax benefit in the third quarter of 2012 includes an incremental tax benefit of \$11.1 million as we determined during the third quarter of 2012 that due to global changes in the business we would not remit certain dividends from non-U.S. jurisdictions. As a result, certain tax attributes were available for carryback to offset prior year tax expense. See Note 8 to our Condensed Consolidated Financial Statements.

We have substantial net operating loss carryforwards in Germany (the equivalent of \$744 million and \$100 million for German corporate and trade tax purposes, respectively, at December 31, 2012). At September 30, 2013, we have concluded that no deferred income tax asset valuation allowance is required to be recognized with respect to such carryforwards, principally because (i) such carryforwards have an indefinite carryforward period, (ii) we have utilized a portion of such carryforwards during the most recent three-year period and (iii) we currently expect to utilize the remainder of such carryforwards over the long term. However, prior to the complete utilization of such carryforwards, particularly if we were to generate losses in our German operations for an extended period of time, it is possible that we might conclude the benefit of such carryforwards would no longer meet the more-likely-than-not recognition criteria, at which point we would be required to recognize a valuation allowance against some or all of the then-remaining tax benefit associated with the carryforwards.

Nine months ended September 30, 2013 compared to the nine months ended September 30, 2012

	Nine months ended September 30,			
	2012		2013	
	(Dollars in millions)			
Net sales	\$ 1,579.5	100%	\$ 1,363.8	100%
Cost of sales	1,068.7	68	1,303.1	96
Gross margin	510.8	32	60.7	4
Other operating expense, net	152.3	9	192.3	14
Income (loss) from operations	\$ 358.5	23%	\$ (131.6)	(10)%

	% Change		
TiO ₂ operating statistics:			
Sales volumes*	368	397	8%
Production volumes*	356	359	1%
Percentage change in net sales:			

TiO ₂ product pricing	(21)%
TiO ₂ sales volumes	8
TiO ₂ product mix	(2)
Changes in currency exchange rates	1
Total	(14)%

*Thousands of metric tons

Net sales Net sales in the nine months ended September 30, 2013 decreased 14%, or \$215.7 million, compared to the nine months ended September 30, 2012 primarily due to the net effects of a 21% decrease in average TiO₂ selling prices (which decreased

net sales by approximately \$332 million) and an 8% increase in sales volumes (which increased net sales by approximately \$126 million). TiO₂ selling prices will increase or decrease generally as a result of competitive market pressures, changes in the relative level of supply and demand as well as changes in raw material and other manufacturing costs.

Our sales volumes increased 8% in the first nine months of 2013 as compared to the first nine months of 2012 due to increased customer demand primarily in European and certain export markets, partially offset by decreased demand in North American markets. In addition, we estimate the favorable effect of changes in currency exchange rates increased our net sales by approximately \$10 million as compared to the first nine months of 2012.

Cost of sales Cost of sales increased \$234.4 million or 22% in the nine months ended September 30, 2013 compared to the same period in 2012 due to the net impact of higher raw material costs of approximately \$108 million (primarily feedstock ore), an 8% increase in sales volumes, a 1% increase in production volumes and currency fluctuations (primarily the euro). Our cost of sales per metric ton of TiO₂ sold in the first half of 2013 was significantly higher than TiO₂ sold in the first half of 2012, as a substantial portion of the TiO₂ products we sold in the first quarter of 2012 (and a portion of the TiO₂ products we sold in the second quarter of 2012) was produced with lower-cost feedstock ore purchased in 2011, while a substantial portion of the TiO₂ products we sold in the first quarter of 2013 (and a portion of the TiO₂ products we sold in the second quarter of 2013) was produced with higher-cost feedstock ore purchased in 2012. As expected, the cost of sales per metric ton of TiO₂ sold in the third quarter of 2013 was lower than the cost of sales per metric ton of TiO₂ sold in the third quarter of 2012 primarily due to the lower feedstock ore costs as discussed and quantified above. Cost of sales as a percentage of net sales increased to 96% in the first nine months of 2013 compared to 68% in the same period of 2012 primarily due to the net effects of higher raw materials costs and to approximately \$25 million of unabsorbed fixed production costs which were charged directly to cost of sales in 2012, as discussed above.

Other operating expense, net Other operating expense in the first nine months of 2013 includes a third quarter litigation settlement charge of \$35 million. See Note 12 to our Condensed Consolidated Financial Statements.

Gross margin and income (loss) from operations Income (loss) from operations decreased by \$490.1 million from income of \$358.5 million in the first nine months of 2012 to a loss of \$131.6 million in the first nine months of 2013.

Income (loss) from operations as a percentage of net sales decreased to (10)% in the first nine months of 2013 from 23% in the same period for 2012. This decrease was driven by the decline in gross margin, which decreased to 4% for the first nine months of 2013 compared to 32% for the same period in 2012, and the third quarter 2013 litigation settlement charge discussed above. As discussed and quantified above, our gross margin has decreased primarily due to the net effects of lower selling prices, higher manufacturing costs (primarily raw materials), higher sales volumes and lower unabsorbed fixed costs related to higher production volumes in 2013 over 2012. Additionally, changes in currency exchange rates have negatively affected our gross margin and income from operations. We estimate that changes in currency exchange rates decreased income from operations by approximately \$7 million in the first nine months of 2013 as compared to the same period in 2012.

Other non-operating income (expense) We recognized an aggregate \$8.9 million pre-tax charge, consisting of the write-off of unamortized original issue discount costs and deferred financing costs, in the first and third quarters of 2013 related to the voluntary prepayment of our term loan by \$290 million in the first quarter of 2013 and the remaining \$100 million in the third quarter of 2013. See Note 7 to our Condensed Consolidated Financial Statements.

We recognized an aggregate \$7.2 million pre-tax charge in the second quarter of 2012 related to the early extinguishment of our remaining Senior Secured Notes.

Interest expense decreased \$3.4 million from \$20.0 million in the nine months ended September 30, 2012 to \$16.6 million in the nine months ended September 30, 2013 primarily due to lower average debt levels in 2013.

Interest and dividend income decreased \$5.7 million to \$.9 million in the nine months ended September 30, 2013 primarily due to lower balances available for investment, principally related to our loan to Valhi which was completely repaid in December 2012. Interest income on our loan to Valhi was \$5.2 million in the nine months ended September 30, 2012.

Income tax expense (benefit) We recognized an income tax benefit of \$51.3 million in the first nine months of 2013 compared to an income tax provision of \$101.3 million in the same period last year. This difference is due in part to our decreased earnings in 2013. In addition, our income tax benefit in the third quarter of 2012 includes an incremental tax benefit of \$11.1 million

as we determined that due to global changes in the business we would not remit certain dividends from non-U.S. jurisdictions. See Note 8 to our Condensed Consolidated Financial Statements for a tabular reconciliation of our statutory income tax provision (benefit) to our actual tax provision (benefit).

Effects of Currency Exchange Rates

We have substantial operations and assets located outside the United States (primarily in Germany, Belgium, Norway and Canada). The majority of our sales from non-U.S. operations are denominated in currencies other than the U.S. dollar, principally the euro, other major European currencies and the Canadian dollar. A portion of our sales generated from our non-U.S. operations is denominated in the U.S. dollar. Certain raw materials used worldwide, primarily titanium-containing feedstocks, are purchased in U.S. dollars, while labor and other production costs are purchased primarily in local currencies. Consequently, the translated U.S. dollar value of our non-U.S. sales and operating results are subject to currency exchange rate fluctuations which may favorably or unfavorably impact reported earnings and may affect the comparability of period-to-period operating results. In addition to the impact of the translation of sales and expenses over time, our non-U.S. operations also generate currency transaction gains and losses which primarily relate to the difference between the currency exchange rates in effect when non-local currency sales or operating costs are initially accrued and when such amounts are settled with the non-local currency.

Overall, we estimate that fluctuations in currency exchange rates had the following effects on our sales and income from operations for the periods indicated.

Impact of changes in currency exchange rates

Three months ended September 30, 2013 vs. September 30, 2012

	Transaction gains/(losses) recognized			Translation gain/loss impact of rate changes	Total currency impact 2013 vs. 2012
	2012	2013	Change		
(in millions)					
Impact on:					
Net sales	\$	\$	\$	\$ 12	\$ 12
Income from operations	(1)		1		1

Impact of changes in currency exchange rates

Nine months ended September 30, 2013 vs. September 30, 2012

	Transaction gains/(losses) recognized			Translation gain/loss impact of rate changes	Total currency impact 2013 vs. 2012
	2012	2013	Change		
(in millions)					
Impact on:					

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Net sales	\$	\$	\$	\$	10	\$	10
Income from operations		(1)	(1)	(6)	(7)		
Outlook							

During the first nine months of 2013 we operated our production facilities at 88% of practical capacity, which was a higher utilization rate as compared to the last three quarters of 2012. Assuming economic conditions do not deteriorate in the various regions of the world in the remainder of 2013, we would expect our sales volumes to continue to be higher in 2013 as compared to 2012. We will continue to monitor current and anticipated near-term customer demand levels and align our production and inventories accordingly.

We have seen some moderation in the cost of TiO₂ feedstock ore procured in 2013; however, these reductions did not begin to be significantly reflected in our cost of sales until the third quarter of 2013. As expected, our cost of sales per metric ton of TiO₂ sold in the third quarter of 2013 was lower than the cost of sales per metric ton of TiO₂ sold in the third quarter of 2012, primarily due to the lower feedstock ore costs, and our cost of sales per metric ton of TiO₂ sold in the fourth quarter of 2013 is similarly expected to be lower than the cost of sales per metric ton of TiO₂ sold in the fourth quarter of 2012. Consequently, our cost of sales per metric ton of TiO₂ sold in the first half of 2013 was significantly higher than what we expect our cost of sales per metric ton of TiO₂ to be in the

second half of 2013, as a substantial portion of the TiO₂ products we sold in the first half of 2013 was produced with the higher-cost feedstock ore procured in 2012. Although the cost of feedstock ore has and continues to moderate, such reductions have been inadequate to compensate for the decline in selling prices for our products over the past year. We started 2013 with selling prices 16% lower than the beginning of 2012, and prices declined by an additional 7% in the first quarter of 2013. After only moderate movement in the second and third quarters of 2013, our average selling prices at the end of the third quarter are 7% below prices at the end of 2012. In the second quarter of 2013, we announced price increases for our TiO₂ products in all of our markets, implementation of which began in June 2013.

In the third quarter of 2013, we notified customers of additional price increases to be implemented beginning in October 2013. Industry data indicates that overall TiO₂ inventory held by producers has been significantly decreased and we believe most customers hold very low inventories of TiO₂ with many operating on a just-in-time basis. As a result lead times for delivery are increasing. With the strong sales volumes experienced in the first nine months of the year, we continue to see evidence of improvement in demand for our TiO₂ products, which we believe will support implementation of additional selling price increases in the near term. The extent to which we will be able to achieve these and other possible additional price increases during the remainder of 2013 and into 2014 will depend on market conditions.

Overall, we expect that income (loss) from operations in 2013 will be significantly lower as compared to 2012, but we also expect income from operations in the fourth quarter of 2013 will improve from the quarterly levels in the first nine months of the year. Our income from operations in the first nine months of 2012 was positively affected by the sale in the first half of 2012 of TiO₂ produced with lower-cost feedstock ore purchased in 2011, while our loss from operations in the first nine months of 2013 was negatively impacted by the sale in the first half of 2013 of TiO₂ produced with higher-cost feedstock ore purchased in 2012, as well as the third quarter litigation settlement charge.

The negative effect of such higher-cost feedstock ore and the legal settlement charge on our full year 2013 operating results is expected to more than offset any favorable effect of higher sales and production volumes that would result assuming demand levels continue to improve, as well as the favorable impact of increases in our selling prices that we may be able to achieve during the remainder of 2013.

Due to the constraints, high capital costs and extended lead time associated with adding significant new TiO₂ production capacity, especially for premium grades of TiO₂ products produced from the chloride process, we believe increased and sustained profit margins will be necessary to financially justify major expansions of TiO₂ production capacity required to meet expected future growth in demand. As a result of customer decisions over the last year and the resulting adverse effect on global TiO₂ pricing, industry projects to increase TiO₂ production capacity have been cancelled or deferred indefinitely. Given the lead time required for such production capacity expansions, we expect a prolonged shortage of TiO₂ products will occur as economic conditions improve and global demand levels for TiO₂ continue to increase.

Our expectations as to the future of the TiO₂ industry are based upon a number of factors beyond our control, including worldwide growth of gross domestic product, competition in the marketplace, continued operation of competitors, unexpected or earlier-than-expected capacity additions or reductions and technological advances. If actual developments differ materially from our expectations, our results of operations could be unfavorably affected.

LIQUIDITY AND CAPITAL RESOURCES

Consolidated cash flows

Operating activities

Trends in cash flows as a result of our operating activities (excluding the impact of significant asset dispositions and relative changes in assets and liabilities) are generally similar to trends in our earnings.

Cash provided by operating activities was \$57.5 million in the first nine months of 2012 compared to \$60.8 million in the first nine months of 2013. This \$3.3 million increase in the amount of cash provided was primarily due to the net effects of the following:

- lower income from operations in 2013 of \$490.1 million;
- lower net cash used in 2013 of \$382.4 million associated with relative changes in our inventories, receivables, payables and accruals, primarily due to the relative decrease in our inventories as discussed below;

- higher net distributions from our TiO₂ manufacturing joint venture in 2013 of \$34.1 million, primarily due to the timing of the joint venture's working capital needs;
- lower net cash paid for income taxes in 2013 of \$51.0 million resulting from our decreased profitability; and
- lower cash paid for interest in 2013 of \$13.3 million, primarily due to the timing of 2012 interest payments on our Senior Secured Notes redeemed in June 2012.

Changes in working capital were affected by accounts receivable and inventory changes. As shown below:

- Our average days sales outstanding, or DSO, increased from December 31, 2012 to September 30, 2013, due to higher average daily net sales resulting from higher sales volumes partially offset by lower selling prices; and
- Our average days sales in inventory, or DSI, decreased from December 31, 2012 to September 30, 2013 principally due to lower inventory raw material costs and lower inventory volumes in 2013.

For comparative purposes, we have also provided comparable prior year numbers below.

	December 31,	September 30,	December 31,	September 30,
	2011	2012	2012	2013
DSO	55 days	60 days	61 days	67 days
DSI	104 days	79 days	102 days	57 days
Investing activities				

Our capital expenditures of \$45.5 million and \$49.9 million in the nine months ended September 30, 2012 and 2013, respectively, were primarily to maintain and improve the cost-effectiveness of our existing manufacturing facilities.

Financing activities

During the nine months ended September 30, 2013, we:

- voluntarily prepaid \$390.0 million principal amount on our term loan;
- borrowed \$190.0 million under our new note payable with Contran and subsequently repaid \$15.0 million;

- borrowed \$90.3 million under our North American credit facility and subsequently repaid \$44.1 million;
 - borrowed 10 million (\$12.8 million when borrowed) on our European credit facility and subsequently repaid 20 million (\$26.5 million when repaid);
 - borrowed \$1.8 million from a Canadian economic development agency;
 - purchased 49,000 shares of our common stock in open market transactions for \$.7 million; and
 - paid quarterly dividends to stockholders aggregating \$.45 per share (\$52.2 million).
- Outstanding debt obligations

At September 30, 2013, our consolidated debt comprised:

- \$175.0 million under our note payable to Contran due in June 2018;
 - \$46.2 million under our North American credit facility due in June 2017; and
 - approximately \$2.8 million of other indebtedness.
- Our North American and European revolvers and our note payable to Contran contain a number of covenants and restrictions which, among other things, restrict our ability to incur additional debt, incur liens, pay dividends or merge or consolidate with, or sell or transfer substantially all of our assets to, another entity, and contains other provisions and restrictive covenants customary in lending transactions of this type. Our European revolving credit facility also requires the maintenance of certain financial ratios. Certain of

our credit agreements contain provisions which could result in the acceleration of indebtedness prior to their stated maturity for reasons other than defaults for failure to comply with typical financial or payment covenants. For example, certain credit agreements allow the lender to accelerate the maturity of the indebtedness upon a change of control (as defined in the agreement) of the borrower. In addition, certain credit agreements could result in the acceleration of all or a portion of the indebtedness following a sale of assets outside the ordinary course of business.

We are in compliance with all of our debt covenants at September 30, 2013. We believe that we will be able to continue to comply with the financial covenants contained in our credit facilities through their maturity; however if future operating results differ materially from our expectations we may be unable to maintain compliance. In such an event, we believe we have alternate sources of liquidity, including cash on hand and borrowings under our North American revolver or additional borrowings from Contran (neither of which contain any financial maintenance covenants) in order to adequately address any compliance issues which might arise.

Our assets consist primarily of investments in operating subsidiaries, and our ability to service parent-level obligations depends in part on the distribution of earnings of our subsidiaries, whether in the form of dividends, advances or payments on account of intercompany obligations or otherwise. Our North American revolving credit facility is collateralized by, among other things, a first priority lien on the borrower's trade receivables and inventories, all or a portion of the common stock or ownership interests in certain of our subsidiaries and a \$362.1 million unsecured promissory note issued by our wholly-owned subsidiary, Kronos International, Inc. Our European revolving credit facility is collateralized by, among other things, the accounts receivable and inventories of the borrowers plus a limited pledge of all the other assets of the Belgian borrower. Our note payable to Contran is unsecured.

See Note 7 to our Condensed Consolidated Financial Statements.

Future cash requirements

Liquidity

Our primary source of liquidity on an ongoing basis is cash flows from operating activities which is generally used to (i) fund working capital expenditures, (ii) repay any short-term indebtedness incurred for working capital purposes and (iii) provide for the payment of dividends. From time-to-time we will incur indebtedness, generally to (i) fund short-term working capital needs, (ii) refinance existing indebtedness or (iii) fund major capital expenditures or the acquisition of other assets outside the ordinary course of business. We will also from time-to-time sell assets outside the ordinary course of business and use the proceeds to (i) repay existing indebtedness, (ii) make investments in marketable and other securities, (iii) fund major capital expenditures or the acquisition of other assets outside the ordinary course of business or (iv) pay dividends.

The TiO₂