

WORTHINGTON INDUSTRIES INC

Form 10-Q

January 09, 2018

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended November 30, 2017

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 001-08399

WORTHINGTON INDUSTRIES, INC.

(Exact name of registrant as specified in its charter)

Ohio

31-1189815

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

200 Old Wilson Bridge Road, Columbus, Ohio

43085

(Address of principal executive offices)

(Zip Code)

(614) 438-3210

(Registrant's telephone number, including area code)

Not Applicable

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

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Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of large accelerated filer, accelerated filer, smaller reporting company, and emerging growth company in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

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

Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS DURING THE PRECEDING FIVE YEARS:

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.

Yes No

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. On December 29, 2017, the number of Common Shares, without par value, issued and outstanding was 61,592,566.

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SAFE HARBOR STATEMENT

Selected statements contained in this Quarterly Report on Form 10-Q, including, without limitation, in PART I Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations, constitute forward-looking statements as that term is used in the Private Securities Litigation Reform Act of 1995 (the Act). Forward-looking statements reflect our current expectations, estimates or projections concerning future results or events. These statements are often identified by the use of forward-looking words or phrases such as believe, expect, anticipate, may, could, intend, estimate, plan, foresee, likely, will, should or other similar words or phrases. These forward-looking statements include, without limitation, statements relating to:

outlook, strategy or business plans;
future or expected growth, growth potential, forward momentum, performance, competitive position, sales, volumes, cash flows, earnings, balance sheet strengths, debt, financial condition or other financial measures;
pricing trends for raw materials and finished goods and the impact of pricing changes;
demand trends for us or our markets;
additions to product lines and opportunities to participate in new markets;
expected benefits from Transformation and innovation efforts and the ability to improve performance and competitive position at our operations;
anticipated working capital needs, capital expenditures and asset sales;
anticipated improvements and efficiencies in costs, operations, sales, inventory management, sourcing and the supply chain and the results thereof;
projected profitability potential;
the ability to successfully integrate AMTROL and the expected benefits, costs and results from the acquisition of AMTROL;
the ability to make acquisitions and the projected timing, results, benefits, costs, charges and expenditures related to acquisitions, newly-created joint ventures, headcount reductions and facility dispositions, shutdowns and consolidations;
the anticipated impact of the pending sale of the WAVE international business;
projected capacity and the alignment of operations with demand;
the ability to operate profitably and generate cash in down markets;
the ability to maintain margins and capture and maintain market share and to develop or take advantage of future opportunities, customer initiatives, new businesses, new products and new markets;
expectations for Company and customer inventories, jobs and orders;
expectations for the economy and markets or improvements therein;
expectations for generating improving and sustainable earnings, earnings potential, margins or shareholder value;
effects of judicial rulings; and
other non-historical matters.

Because they are based on beliefs, estimates and assumptions, forward-looking statements are inherently subject to risks and uncertainties that could cause actual results to differ materially from those projected. Any number of factors could affect actual results, including, without limitation, those that follow:

the effect of national, regional and global economic conditions generally and within major product markets, including a recurrent slowing economy;
the effect of conditions in national and worldwide financial markets;
lower oil prices as a factor in demand for products;
product demand and pricing;
changes in product mix, product substitution and market acceptance of our products;
fluctuations in the pricing, quality or availability of raw materials (particularly steel), supplies, transportation, utilities and other items required by operations;
effects of facility closures and the consolidation of operations;
the effect of financial difficulties, consolidation and other changes within the steel, automotive, construction, oil and gas, and other industries in which we participate;
failure to maintain appropriate levels of inventories;
financial difficulties (including bankruptcy filings) of original equipment manufacturers, end-users and customers, suppliers, joint venture partners and others with whom we do business;

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the ability to realize targeted expense reductions from headcount reductions, facility closures and other cost reduction efforts;
the ability to realize cost savings and operational, sales and sourcing improvements and efficiencies, and other expected benefits from Transformation initiatives, on a timely basis;
the overall success of, and the ability to integrate, newly-acquired businesses and joint ventures, maintain and develop their customers, and achieve synergies and other expected benefits and cost savings therefrom;
the successful completion of the single, integrated sale of the Armstrong World Industries international business and the WAVE international business;
capacity levels and efficiencies, within facilities, within major product markets and within the industries as a whole;
the effect of disruption in the business of suppliers, customers, facilities and shipping operations due to adverse weather, casualty events, equipment breakdowns, civil unrest, international conflicts, terrorist activities or other causes;
changes in customer demand, inventories, spending patterns, product choices, and supplier choices;
risks associated with doing business internationally, including economic, political and social instability, foreign currency exchange rate exposure and the acceptance of our products in global markets;
the ability to improve and maintain processes and business practices to keep pace with the economic, competitive and technological environment;
the outcome of adverse claims experience with respect to workers' compensation, product recalls or product liability, casualty events or other matters;
deviation of actual results from estimates and/or assumptions used by us in the application of our critical accounting policies;
level of imports and import prices in our markets;
the impact of judicial rulings and governmental regulations, both in the United States and abroad, including those adopted by the United States Securities and Exchange Commission and other governmental agencies as contemplated by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010;
the effect of healthcare laws in the United States and potential changes for such laws which may increase our healthcare and other costs and negatively impact our operations and financial results;
the impact of the recently-enacted Tax Cuts and Jobs Act, including a reduction in the corporate tax rate and the related impact on the Company's deferred tax balances as well as the impact of the one-time mandatory tax on previously deferred foreign earnings;
cyber security risks; and
other risks described from time to time in the filings of Worthington Industries, Inc. with the United States Securities and Exchange Commission, including those described in PART I Item 1A. Risk Factors of our Annual Report on Form 10-K for the fiscal year ended May 31, 2017.

We note these factors for investors as contemplated by the Act. It is impossible to predict or identify all potential risk factors. Consequently, you should not consider the foregoing list to be a complete set of all potential risks and uncertainties. Any forward-looking statements in this Quarterly Report on Form 10-Q are based on current information as of the date of this Quarterly Report on Form 10-Q, and we assume no obligation to correct or update any such statements in the future, except as required by applicable law.

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****WORTHINGTON INDUSTRIES, INC.****CONSOLIDATED BALANCE SHEETS****(In thousands)****(Unaudited)**

	November 30, 2017	May 31, 2017
Assets		
Current assets:		
Cash and cash equivalents	\$ 122,214	\$ 278,081
Receivables, less allowances of \$3,127 and \$3,444 at November 30, 2017 and May 31, 2017, respectively	507,704	486,730
Inventories:		
Raw materials	228,568	185,001
Work in process	108,260	95,630
Finished products	79,180	73,303
Total inventories	416,008	353,934
Income taxes receivable	10,858	7,164
Assets held for sale	3,740	9,654
Prepaid expenses and other current assets	51,204	55,406
Total current assets	1,111,728	1,190,969
Investments in unconsolidated affiliates	213,814	208,591
Goodwill	350,117	247,673
Other intangible assets, net of accumulated amortization of \$71,580 and \$63,134 at November 30, 2017 and May 31, 2017, respectively	239,934	82,781
Other assets	28,369	24,841
Property, plant and equipment:		
Land	27,381	22,077
Buildings and improvements	311,685	297,951
Machinery and equipment	1,035,787	961,542
Construction in progress	34,015	27,616
Total property, plant and equipment	1,408,868	1,309,186
Less: accumulated depreciation	781,117	738,697
Total property, plant and equipment, net	627,751	570,489

Total assets	\$ 2,571,713	\$ 2,325,344
Liabilities and equity		
Current liabilities:		
Accounts payable	\$ 363,032	\$ 368,071
Short-term borrowings	723	123
Accrued compensation, contributions to employee benefit plans and related taxes	74,404	86,201
Dividends payable	13,815	13,698
Other accrued items	59,255	41,551
Income taxes payable	2,027	4,448
Current maturities of long-term debt	13,193	6,691
Total current liabilities	526,449	520,783
Other liabilities	68,672	61,498
Distributions in excess of investment in unconsolidated affiliate	61,085	63,038
Long-term debt	766,737	571,796
Deferred income taxes, net	105,987	34,300
Total liabilities	1,528,930	1,251,415
Shareholders' equity controlling interest	919,287	951,635
Noncontrolling interests	123,496	122,294
Total equity	1,042,783	1,073,929
Total liabilities and equity	\$ 2,571,713	\$ 2,325,344

See notes to consolidated financial statements.

Table of Contents**WORTHINGTON INDUSTRIES, INC.****CONSOLIDATED STATEMENTS OF EARNINGS****(In thousands, except per share amounts)****(Unaudited)**

	Three Months Ended		Six Months Ended	
	November 30,		November 30,	
	2017	2016	2017	2016
Net sales	\$ 871,266	\$ 727,780	\$ 1,719,503	\$ 1,465,329
Cost of goods sold	731,187	604,977	1,446,646	1,195,244
Gross margin	140,079	122,803	272,857	270,085
Selling, general and administrative expense	89,425	76,487	177,674	157,543
Impairment of goodwill and long-lived assets	8,289		8,289	
Restructuring and other expense (income), net	(9,694)	3,272	(7,390)	4,600
Operating income	52,059	43,044	94,284	107,942
Other income (expense):				
Miscellaneous income, net	1,321	872	1,669	1,735
Interest expense	(10,038)	(7,658)	(18,845)	(15,528)
Equity in net income of unconsolidated affiliates	16,445	27,124	43,751	61,668
Earnings before income taxes	59,787	63,382	120,859	155,817
Income tax expense	18,165	13,515	31,163	37,414
Net earnings	41,622	49,867	89,696	118,403
Net earnings attributable to noncontrolling interests	2,219	3,302	4,759	6,271
Net earnings attributable to controlling interest	\$ 39,403	\$ 46,565	\$ 84,937	\$ 112,132
Basic				
Average common shares outstanding	61,503	62,348	61,976	62,115
Earnings per share attributable to controlling interest	\$ 0.64	\$ 0.75	\$ 1.37	\$ 1.81
Diluted				
Average common shares outstanding	63,468	64,725	64,044	64,599
Earnings per share attributable to controlling interest	\$ 0.62	\$ 0.72	\$ 1.33	\$ 1.74
Common shares outstanding at end of period	60,755	62,562	60,755	62,562

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Cash dividends declared per share	\$	0.21	\$	0.20	\$	0.42	\$	0.40
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See notes to consolidated financial statements.

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	Three Months Ended		Six Months Ended	
	November 30,		November 30,	
	2017	2016	2017	2016
Net earnings	\$ 41,622	\$ 49,867	\$ 89,696	\$ 118,403
Other comprehensive income (loss):				
Foreign currency translation	1,511	(7,517)	17,383	(8,182)
Pension liability adjustment, net of tax			(6)	
Cash flow hedges, net of tax	(2,210)	1,652	(323)	2,277
Other comprehensive income (loss)	(699)	(5,865)	17,054	(5,905)
Comprehensive income	40,923	44,002	106,750	112,498
Comprehensive income attributable to noncontrolling interests	2,139	3,155	5,118	6,128
Comprehensive income attributable to controlling interest	\$ 38,784	\$ 40,847	\$ 101,632	\$ 106,370

See notes to consolidated financial statements.

Table of Contents**WORTHINGTON INDUSTRIES, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS****(In thousands)****(Unaudited)**

	Three Months Ended		Six Months Ended	
	November 30,		November 30,	
	2017	2016	2017	2016
Operating activities:				
Net earnings	\$ 41,622	\$ 49,867	\$ 89,696	\$ 118,403
Adjustments to reconcile net earnings to net cash provided by operating activities:				
Depreciation and amortization	26,283	21,645	51,648	43,476
Impairment of goodwill and long-lived assets	8,289		8,289	
Provision for (benefit from) deferred income taxes	(583)	2,316	7,351	2,336
Bad debt (income) expense	41	232	(21)	151
Equity in net income of unconsolidated affiliates, net of distributions	2,952	(2,824)	(4,803)	1,074
Net (gain) loss on assets	(10,680)	(2,912)	(9,255)	1,484
Stock-based compensation	3,787	3,824	7,194	6,960
Changes in assets and liabilities, net of impact of acquisitions:				
Receivables	(46,097)	(7,156)	16,581	9,798
Inventories	9,871	31,875	(24,825)	(18,523)
Prepaid expenses and other current assets	3,622	(1,737)	4,765	5,425
Other assets	(626)	1,165	(976)	2,411
Accounts payable and accrued expenses	(21,577)	(65,946)	(48,368)	(22,885)
Other liabilities	2,478	950	5,461	2,094
Net cash provided by operating activities	19,382	31,299	102,737	152,204
Investing activities:				
Investment in property, plant and equipment	(23,678)	(14,730)	(41,691)	(31,046)
Acquisitions, net of cash acquired	(523)		(285,028)	
Proceeds from sale of assets	16,312	799	16,739	956
Net cash used by investing activities	(7,889)	(13,931)	(309,980)	(30,090)
Financing activities:				
Net proceeds from (repayments of) short-term borrowings	302	(1,037)	600	(2,154)
Proceeds from long-term debt, net of issuance costs	(594)		197,685	
Principal payments on long-term debt	(220)	(218)	(439)	(437)
	(722)	(2,849)	(3,996)	2,972

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Proceeds from issuance of common shares, net of tax withholdings				
Payments to noncontrolling interests	(3,196)	(6,781)	(3,916)	(6,781)
Repurchase of common shares	(67,448)		(112,524)	
Dividends paid	(13,256)	(12,828)	(26,034)	(24,722)
Net cash provided (used) by financing activities	(85,134)	(23,713)	51,376	(31,122)
Increase (decrease) in cash and cash equivalents	(73,641)	(6,345)	(155,867)	90,992
Cash and cash equivalents at beginning of period	195,855	181,525	278,081	84,188
Cash and cash equivalents at end of period	\$ 122,214	\$ 175,180	\$ 122,214	\$ 175,180

See notes to consolidated financial statements.

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WORTHINGTON INDUSTRIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE A Basis of Presentation

The consolidated financial statements include the accounts of Worthington Industries, Inc. and consolidated subsidiaries (collectively, we, our, Worthington, or the Company). Investments in unconsolidated affiliates accounted for using the equity method. Significant intercompany accounts and transactions are eliminated.

The Company owns controlling interests in the following five joint ventures: Spartan Steel Coating, LLC (Spartan) (52%), TWB Company, L.L.C. (TWB) (55%), Worthington Aritas Basınçlı Kaplar Sanayi (Worthington Aritas) (75%), Worthington Energy Innovations, LLC (WEI) (75%), and Worthington Specialty Processing (WSP) (51%). These joint ventures are consolidated with the equity owned by the other joint venture members shown as noncontrolling interests in our consolidated balance sheets, and their portions of net earnings and other comprehensive income (loss) (OCI) shown as net earnings or comprehensive income attributable to noncontrolling interests in our consolidated statements of earnings and consolidated statements of comprehensive income, respectively.

These unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X of the Securities and Exchange Commission (SEC). Accordingly, they do not include all of the information and notes required by U.S. GAAP for complete financial statements. In the opinion of management, all adjustments, which are of a normal and recurring nature, except those which have been disclosed elsewhere in this Quarterly Report on Form 10-Q, necessary for a fair presentation of the consolidated financial statements for these interim periods, have been included. Operating results for the three and six months ended November 30, 2017 are not necessarily indicative of the results that may be expected for the fiscal year ending May 31, 2018 (fiscal 2018). For further information, refer to the consolidated financial statements and notes thereto included in the Annual Report on Form 10-K for the fiscal year ended May 31, 2017 (fiscal 2017) of Worthington Industries, Inc. (the 2017 Form 10-K).

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

Recently Adopted Accounting Standards

In July 2015, amended accounting guidance was issued regarding the measurement of inventory. The amended guidance requires that inventory accounted for under the first-in, first-out (FIFO) or average cost methods be measured at the lower of cost and net realizable value, where net realizable value represents the estimated selling price of inventory in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. The amended guidance has no impact on inventory accounted for under the last-in, first-out (LIFO) or retail inventory methods. The Company adopted this amended guidance on a prospective basis effective June 1, 2017. The adoption of this guidance did not impact our consolidated financial position or results of operations.

In August 2016, amended accounting guidance was issued to clarify the proper cash flow presentation of certain specific types of cash payments and cash receipts. The Company early adopted this amended guidance on a

prospective basis effective June 1, 2017. The adoption of this guidance did not impact our consolidated statements of cash flows or ongoing financial reporting.

In January 2017, amended accounting guidance was issued to clarify the definition of a business to provide additional guidance to assist in evaluating whether transactions should be accounted for as an acquisition (or disposal) of either an asset or a business. The Company early adopted this amended guidance on a prospective basis effective September 1, 2017. The adoption of this guidance did not impact our consolidated financial position or results of operations.

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In January 2017, amended accounting guidance was issued to simplify the goodwill impairment calculation, by removing Step 2 of the goodwill impairment test. Goodwill impairment will now be the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of the goodwill. The Company early adopted this amended guidance on a prospective basis effective September 1, 2017. The adoption of this guidance did not impact our consolidated financial position or results of operations.

Recently Issued Accounting Standards

In May 2014, new accounting guidance was issued that replaces most existing revenue recognition guidance under U.S. GAAP. The new guidance requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. Subsequently, additional guidance was issued on several areas including guidance intended to improve the operability and understandability of the implementation of principal versus agent considerations and clarifications on the identification of performance obligations and implementation of guidance related to licensing. The new guidance is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. The guidance permits the use of either the retrospective or cumulative effect transition method. We are in the process of evaluating the effect this guidance will have on the presentation of our consolidated financial statements and related disclosures. The scoping and diagnostic phases of the implementation are largely complete and reviews of the Company's contracts are ongoing. While we have not yet identified any material changes in the timing of revenue recognition, our evaluation is ongoing and not complete. The Company will adopt this guidance on June 1, 2018 using the cumulative effect transition method. The Company will continue to monitor any modifications, clarifications, and interpretations by the FASB that may impact its conclusions.

In February 2016, new accounting guidance was issued that replaces most existing lease accounting guidance under U.S. GAAP. Among other changes, the new guidance requires that lease assets and liabilities be recognized on the balance sheet by lessees for those leases classified as operating leases under previous guidance. The new guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted, and the change is to be applied using a modified retrospective approach as of the beginning of the earliest period presented. We are in the process of evaluating the effect this guidance will have on our consolidated financial position, results of operations and cash flows, and we have not determined the effect of the new guidance on our ongoing financial reporting.

In June 2016, new accounting guidance was issued related to the measurement of credit losses on financial instruments. The new guidance changes the impairment model for most financial assets to require measurement and recognition of expected credit losses for financial assets held. The new guidance is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. We are in the process of evaluating the effect this guidance will have on our consolidated financial position and results of operations, however, we do not expect the new guidance to have a material impact on our ongoing financial reporting.

In October 2016, amended accounting guidance was issued that requires the income tax consequences of an intra-entity transfer of an asset other than inventory to be recognized when the transfer occurs. The amended guidance is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption is permitted. We are in the process of evaluating the effect this guidance will have on our consolidated financial position, results of operations and cash flows, and have not determined the effect of the amended guidance on our ongoing financial reporting.

In November 2016, amended accounting guidance was issued that requires amounts generally described as restricted cash and restricted cash equivalents to be included with cash and cash equivalents when reconciling the

beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The amended guidance is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption is permitted. We do not expect the adoption of this amended guidance to have a material impact on our consolidated cash flows.

In March 2017, amended accounting guidance was issued that requires an employer to report the service cost component of pension and postretirement benefits in the same line as other current employee compensation costs. Additionally, other components of net benefit cost are to be presented in the income statement separately from the service cost component and outside of income from operations. The amended guidance is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. We are in the process of evaluating the effect this guidance will have on our consolidated financial position and results of operations, however, we do not expect the new guidance to have a material impact on our ongoing financial reporting.

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In May 2017, amended accounting guidance was issued to provide guidance about which changes to the terms or conditions of a share-based payment award require application of modification accounting. The amended guidance is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption is permitted. We do not expect the adoption of this amended guidance to have a material impact on our consolidated financial position or results of operations.

In August 2017, amended accounting guidance was issued that modifies hedge accounting by making more hedge strategies eligible for hedge accounting, amending presentation and disclosure requirements, and changing how companies assess effectiveness. The intent is to simplify application of hedge accounting and increase transparency of information about an entity's risk management activities. The amended guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. We are in the process of evaluating the effect this guidance will have on our consolidated financial position and results of operations, and have not determined the effect on our ongoing financial reporting.

NOTE B Investments in Unconsolidated Affiliates

Investments in affiliated companies that we do not control, either through majority ownership or otherwise, are accounted for using the equity method. These include ArtiFlex Manufacturing, LLC (ArtiFlex) (50%), Clarkwestern Dietrich Building Systems LLC (ClarkDietrich) (25%), Samuel Steel Pickling Company (31.25%), Serviaceros Planos, S. de R. L. de C.V. (Serviaceros) (50%), Worthington Armstrong Venture (WAVE) (50%), and Zhejiang Nisshin Worthington Precision Specialty Steel Co., Ltd. (10%).

We received distributions from unconsolidated affiliates totaling \$38,948,000 during the six months ended November 30, 2017. We have received cumulative distributions from WAVE in excess of our investment balance, which resulted in an amount recorded within other liabilities on our consolidated balance sheets of \$61,085,000 at November 30, 2017. In accordance with the applicable accounting guidance, we reclassified the negative balance to the liabilities section of our consolidated balance sheet. We will continue to record our equity in the net income of WAVE as a debit to the investment account, and if it becomes positive, it will again be shown as an asset on our consolidated balance sheet. If it becomes probable that any excess distribution may not be returned (upon joint venture liquidation or otherwise), we will recognize any balance classified as a liability as income immediately.

We use the cumulative earnings approach for determining cash flow presentation of distributions from our unconsolidated joint ventures. Distributions received are included in our consolidated statements of cash flows as operating activities, unless the cumulative distributions received, less distributions received in prior periods that were determined to be returns of investment, exceed our portion of the cumulative equity in the net earnings of the joint venture, in which case the excess distributions are deemed to be returns of the investment and are classified as investing activities in our consolidated statements of cash flows.

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Combined financial information for our unconsolidated affiliates is summarized in the tables below:

(in thousands)	November 30, 2017	May 31, 2017
Cash	\$ 50,389	\$ 55,541
Other current assets	553,970	559,021
Noncurrent assets	371,328	361,106
Total assets	\$ 975,687	\$ 975,668
Current liabilities	\$ 139,168	\$ 156,947
Short-term borrowings	16,539	8,172
Current maturities of long-term debt	5,118	5,827
Long-term debt	266,036	268,711
Other noncurrent liabilities	21,637	21,380
Equity	527,189	514,631
Total liabilities and equity	\$ 975,687	\$ 975,668

(in thousands)	Three Months Ended November 30,		Six Months Ended November 30,	
	2017	2016	2017	2016
Net sales	\$ 412,617	\$ 387,192	\$ 855,241	\$ 804,307
Gross margin	71,122	96,541	157,357	220,738
Operating income	34,604	67,365	91,767	161,762
Depreciation and amortization	5,935	6,973	13,128	13,793
Interest expense	2,461	2,151	4,953	4,299
Income tax expense	1,816	3,545	3,164	11,063
Net earnings	30,190	63,444	82,664	149,511

On November 20, 2017, the Company announced that the WAVE joint venture agreed to sell its business and operations in Europe, Middle East, Africa and Asia, to Knauf Group, a family-owned manufacturer of building materials headquartered in Germany. Worthington expects to receive proceeds of approximately \$45,000,000 for its 50% share of the WAVE operations being sold. The transaction is subject to regulatory approvals and other customary closing conditions and is anticipated to close in the middle of calendar 2018. The operations being sold generated a net loss of \$1,703,000 and \$273,000 during the three and six months ended November 30, 2017, respectively. Results for the three and six months ended November 30, 2017 included allocated costs of \$2,263,000 related to the period covering January 1 to August 31, 2017 as a result of a new cost-sharing agreement between the joint venture and its partners. Net assets of the business being sold were approximately \$31,500,000 as of November 30, 2017. These amounts have been included in the tables presented above.

NOTE C Impairment of Goodwill and Long-Lived Assets

During the second quarter of fiscal 2018, the Company determined that indicators of impairment were present with regard to the goodwill and intangible assets of the WEI reporting unit. As a result, these assets were written down to

their estimated fair value resulting in an impairment charge of \$7,325,000. During the second quarter of fiscal 2018, the Company also identified the presence of impairment indicators with regard to vacant land at the oil & gas equipment facility in Bremen, Ohio, resulting in an impairment charge of \$964,000 to write the vacant land down to its estimated fair market value.

NOTE D Restructuring and Other Expense

We consider restructuring activities to be programs whereby we fundamentally change our operations such as closing and consolidating manufacturing facilities or moving manufacturing of a product to another location. Restructuring activities may also involve substantial realignment of the management structure of a business unit in response to changing market conditions.

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A progression of the liabilities associated with our restructuring activities, combined with a reconciliation to the restructuring and other expense financial statement caption, in our consolidated statement of earnings for the six months ended November 30, 2017 is summarized below:

(in thousands)	Beginning Balance	Expense	Payments	Adjustments	Ending Balance
Early retirement and severance	\$ 253	\$ 2,560	\$ (598)	\$ -	\$ 2,215
Facility exit and other costs	536	502	(1,038)	-	-
	\$ 789	3,062	\$ (1,636)	\$ -	\$ 2,215
Net gain on sale of assets		(10,452)			
Restructuring and other income, net		\$ (7,390)			

During the six months ended November 30, 2017, the following actions were taken related to the Company's restructuring activities:

In connection with the acquisition of Amtrol on June 2, 2017, the Company recognized severance expense of \$2,365,000 related to corporate management positions at Amtrol that were eliminated.

In connection with the closure of the Company's stainless steel business, Precision Specialty Metals, Inc. (PSM), the Company recognized facility exit costs of \$580,000 and a net gain on disposal of assets of \$10,595,000 for the sale of the legacy real estate of this business. Net proceeds were \$15,874,000.

In connection with other non-significant restructuring activities, the Company recognized severance expense of \$195,000 and a credit to facility exit costs of \$78,000. The Company also recognized a net loss on disposal of assets of \$143,000.

The total liability associated with our restructuring activities as of November 30, 2017 is expected to be paid in the next twelve months.

NOTE E Contingent Liabilities and Commitments

We are defendants in certain legal actions. In the opinion of management, the outcome of these actions, which is not clearly determinable at the present time, would not have a material adverse effect on our consolidated financial position or future results of operations or cash flows. We believe that environmental issues will not have a material effect on our capital expenditures, consolidated financial position or future results of operations or cash flows.

NOTE F Guarantees

We do not have guarantees that we believe are reasonably likely to have a material current or future effect on our consolidated financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity,

capital expenditures or capital resources. However, as of November 30, 2017, we were party to an operating lease for an aircraft in which we have guaranteed a residual value at the termination of the lease. The maximum obligation under the terms of this guarantee was approximately \$8,819,000 at November 30, 2017. Based on current facts and circumstances, we have estimated the likelihood of payment pursuant to this guarantee is not probable and, therefore, no amount has been recognized in our consolidated financial statements.

We also had in place \$15,877,000 of outstanding stand-by letters of credit issued to third-party service providers at November 30, 2017. The fair value of these guarantee instruments, based on premiums paid, was not material and no amounts were drawn against them at November 30, 2017.

NOTE G Debt and Receivables Securitization

On July 28, 2017, we issued \$200,000,000 aggregate principal amount of senior unsecured notes due August 1, 2032 (the 2032 Notes). The 2032 Notes bear interest at a rate of 4.300%. The 2032 Notes were sold to the public at 99.901% of the principal amount thereof, to yield 4.309% to maturity. We used a portion of the net proceeds from the offering to repay amounts then outstanding under our multi-year revolving credit facility and amounts then outstanding under our revolving trade accounts receivable securitization facility, both of which are described in more detail below. We entered into an interest rate swap in June 2017, in anticipation of the issuance of the 2032 Notes. The interest rate swap had a notional amount of \$150,000,000 to hedge the risk of changes in the semi-annual interest rate payments attributable to changes in the benchmark interest rate during the several days leading up to the issuance of the 2032 Notes. Upon pricing of the 2032 Notes, the derivative instrument was settled resulting in a gain of approximately \$3,098,000, which was reflected in accumulated other comprehensive income (AOCI). Approximately \$2,116,000 and \$198,000 were allocated to debt issuance costs and the debt discount. The debt issuance costs and the debt discount were recorded on the consolidated balance sheet within long-term debt as a contra-liability. The unamortized portion of the debt issuance costs and debt discount was \$2,069,000 and \$194,000, respectively, at November 30, 2017.

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We maintain a \$500,000,000 multi-year revolving credit facility (the Credit Facility) with a group of lenders that matures in April 2020. Borrowings under the Credit Facility typically have maturities of less than one year. However, we can extend the term of amounts borrowed by renewing these borrowings for the term of the Credit Facility. We have the option to borrow at rates equal to an applicable margin over the LIBOR, Prime rate or Fed Funds rate. The applicable margin is determined by our credit rating. There were no borrowings outstanding under the Credit Facility at November 30, 2017. As discussed in NOTE F Guarantees, we provided \$15,877,000 in stand-by letters of credit for third-party beneficiaries as of November 30, 2017. While not drawn against at November 30, 2017, \$14,495,000 of these stand-by letters of credit were issued against availability under the Credit Facility, leaving \$485,505,000 available under the Credit Facility at November 30, 2017.

We also maintain a \$100,000,000 revolving trade accounts receivable securitization facility (the AR Facility). The AR Facility has been available throughout fiscal 2018 to date and was available throughout fiscal 2017. The AR Facility expires in January 2018; however, we are currently in the process of renewing this agreement and expect to renew this facility prior to its expiration. Pursuant to the terms of the AR Facility, certain of our subsidiaries sell their accounts receivable without recourse, on a revolving basis, to Worthington Receivables Corporation (WRC), a wholly-owned, consolidated, bankruptcy-remote subsidiary. In turn, WRC may sell without recourse, on a revolving basis, up to \$100,000,000 of undivided ownership interests in this pool of accounts receivable to a third-party bank. We retain an undivided interest in this pool and are subject to risk of loss based on the collectability of the receivables from this retained interest. Because the amount eligible to be sold excludes receivables more than 90 days past due, receivables offset by an allowance for doubtful accounts due to bankruptcy or other cause, concentrations over certain limits with specific customers and certain reserve amounts, we believe additional risk of loss is minimal. As of November 30, 2017, no undivided ownership interests in this pool of accounts receivable had been sold.

NOTE H Other Comprehensive Income

The following table summarizes the tax effects on each component of OCI for the three months ended November 30:

(in thousands)	2017			2016		
	Before-Tax	Tax	Net-of-Tax	Before-Tax	Tax	Net-of-Tax
Foreign currency translation	\$ 1,511	\$ -	\$ 1,511	\$(7,517)	\$ -	\$(7,517)
Pension liability adjustment	-	-	-	-	-	-
Cash flow hedges	(3,495)	1,285	(2,210)	2,047	(395)	1,652
Other comprehensive loss	\$ (1,984)	\$ 1,285	\$ (699)	\$(5,470)	\$(395)	\$(5,865)

The following table summarizes the tax effects on each component of OCI for the six months ended November 30:

(in thousands)	2017			2016		
	Before-Tax	Tax	Net-of-Tax	Before-Tax	Tax	Net-of-Tax
Foreign currency translation	\$ 17,383	\$ -	\$ 17,383	\$(8,182)	\$ -	\$(8,182)
Pension liability adjustment	-	(6)	(6)	-	-	-
Cash flow hedges	(502)	179	(323)	3,135	(858)	2,277

Other comprehensive income (loss)	\$ 16,881	\$ 173	\$ 17,054	\$(5,047)	\$(858)	\$ (5,905)
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Table of Contents**NOTE I Changes in Equity**

The following table summarizes the changes in equity by component and in total for the six months ended November 30, 2017:

(in thousands)	Controlling Interest Accumulated Other			Total	Non controlling	
	Additional Paid-in Capital	Comprehensive Loss, Net of Tax	Retained Earnings		Interests	Total
Balance at May 31, 2017	\$ 303,391	\$ (27,775)	\$ 676,019	\$ 951,635	\$ 122,294	\$ 1,073,929
Net earnings	-	-	84,937	84,937	4,759	89,696
Other comprehensive income	-	16,695	-	16,695	359	17,054
Common shares issued, net of withholding tax	(3,996)	-	-	(3,996)	-	(3,996)
Common shares in NQ plans	886	-	-	886	-	886
Stock-based compensation	7,991	-	-	7,991	-	7,991
Purchases and retirement of common shares	(11,480)	-	(101,044)	(112,524)	-	(112,524)
Cash dividends declared	-	-	(26,337)	(26,337)	-	(26,337)
Dividends to noncontrolling interest	-	-	-	-	(3,916)	(3,916)
Balance at November 30, 2017	\$ 296,792	\$ (11,080)	\$ 633,575	\$ 919,287	\$ 123,496	\$ 1,042,783

The following table summarizes the changes in accumulated other comprehensive loss for the six months ended November 30, 2017:

(in thousands)	Foreign Currency Translation	Pension Liability Adjustment	Cash Flow Hedges	Accumulated Other Comprehensive Loss
Balance as of May 31, 2017	\$ (17,358)	\$ (14,819)	\$ 4,402	\$ (27,775)
Other comprehensive income before reclassifications	17,024	-	8,912	25,936
Reclassification adjustments to income (a)	-	-	(9,414)	(9,414)
Income taxes	-	(6)	179	173
Balance as of November 30, 2017	\$ (334)	\$ (14,825)	\$ 4,079	\$ (11,080)

(a)

The statement of earnings classification of amounts reclassified to income for cash flow hedges is disclosed in
NOTE O Derivative Instruments and Hedging Activities.

Table of Contents**NOTE J Stock-Based Compensation****Non-Qualified Stock Options**

During the six months ended November 30, 2017, we granted non-qualified stock options covering a total of 90,200 common shares under our stock-based compensation plans. The option price of \$47.76 per share was equal to the market price of the underlying common shares at the grant date. The fair value of these stock options, based on the Black-Scholes option-pricing model, calculated at the grant date, was \$14.99 per share. The calculated pre-tax stock-based compensation expense for these stock options, after an estimate for forfeitures, is \$1,203,000 and will be recognized on a straight-line basis over the three-year vesting period. The following assumptions were used to value these stock options:

Dividend yield	1.81%
Expected volatility	36.65%
Risk-free interest rate	1.98%
Expected term (years)	6.0

Expected volatility is based on the historical volatility of our common shares and the risk-free interest rate is based on the United States Treasury strip rate for the expected term of the stock options. The expected term was developed using historical exercise experience.

Service-Based Restricted Common Shares

During the six months ended November 30, 2017, we granted an aggregate of 159,700 service-based restricted common shares under our stock-based compensation plans. The fair value of these restricted common shares was equal to the weighted average closing market price of the underlying common shares on the respective dates of grant, or \$48.15 per share. The calculated pre-tax stock-based compensation expense for these restricted common shares, after an estimate for forfeitures, is \$6,964,000 and will be recognized on a straight-line basis over the three-year service-based vesting period.

Performance Share Awards

We have awarded performance shares to certain key employees under our stock-based compensation plans. These performance shares are earned based on the level of achievement with respect to corporate targets for cumulative corporate economic value added, earnings per share growth and, in the case of business unit executives, business unit operating income targets for the three-year periods ending May 31, 2018, 2019 and 2020. These performance share awards will be paid, to the extent earned, in common shares of the Company in the fiscal quarter following the end of the applicable three-year performance period. The fair values of our performance shares are determined by the closing market prices of the underlying common shares at the respective grant dates of the performance shares and the pre-tax stock-based compensation expense is based on our periodic assessment of the probability of the targets being achieved and our estimate of the number of common shares that will ultimately be issued. During the six months ended November 30, 2017, we granted performance share awards covering an aggregate of 54,700 common shares (at target levels). The calculated pre-tax stock-based compensation expense for these performance shares is \$2,768,000 and will be recognized over the three-year performance period.

NOTE K Income Taxes

Income tax expense for the six months ended November 30, 2017 and 2016 reflected estimated annual effective income tax rates of 30.0% and 28.5%, respectively. The annual effective income tax rates exclude any impact from the inclusion of net earnings attributable to noncontrolling interests in our consolidated statements of earnings. Net earnings attributable to noncontrolling interests are primarily a result of our WSP, Spartan, Worthington Aritas, and TWB consolidated joint ventures. The earnings attributable to the noncontrolling interests in WSP, Spartan and TWB's U.S. operations do not generate tax expense to Worthington since the investors in WSP, Spartan and TWB's U.S. operations are taxed directly based on the earnings attributable to them. The tax expense of Worthington Aritas (a foreign corporation) and TWB's wholly-owned foreign corporations is reported in our consolidated tax expense. Management is required to estimate the annual effective income tax rate based upon its forecast of annual pre-tax income for domestic and foreign operations. Our actual effective income tax rate for fiscal 2018 could be materially different from the forecasted rate as of November 30, 2017.

Table of Contents**NOTE L Earnings per Share**

The following table sets forth the computation of basic and diluted earnings per share attributable to controlling interest for the periods presented:

(in thousands, except per share amounts)	Three Months Ended		Six Months Ended	
	November 30, 2017	2016	November 30, 2017	2016
Numerator (basic & diluted):				
Net earnings attributable to controlling interest -income available to common shareholders	\$ 39,403	\$ 46,565	\$ 84,937	\$ 112,132
Denominator:				
Denominator for basic earnings per share attributable to controlling interest weighted average common shares	61,503	62,348	61,976	62,115
Effect of dilutive securities	1,965	2,377	2,068	2,484
Denominator for diluted earnings per share attributable to controlling interest adjusted weighted average common shares	63,468	64,725	64,044	64,599
Basic earnings per share attributable to controlling interest	\$ 0.64	\$ 0.75	\$ 1.37	\$ 1.81
Diluted earnings per share attributable to controlling interest	\$ 0.62	\$ 0.72	\$ 1.33	\$ 1.74

Stock options covering 195,774 and 110,354 common shares for the three months ended November 30, 2017 and 2016, respectively, and 76,605 and 92,923 common shares for the six months ended November 30, 2017 and 2016, respectively, have been excluded from the computation of diluted earnings per share because the effect of their inclusion would have been anti-dilutive for those periods.

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The following table presents summarized financial information for our reportable segments as of, and for the periods presented:

(in thousands)	Three Months Ended November 30,		Six Months Ended November 30,	
	2017	2016	2017	2016
Net sales				
Steel Processing	\$ 538,390	\$ 508,806	\$ 1,081,881	\$ 1,014,480
Pressure Cylinders	300,862	194,661	570,673	399,870
Engineered Cabs	30,404	22,463	62,350	48,044
Other	1,610	1,850	4,599	2,935
Total net sales	\$ 871,266	\$ 727,780	\$ 1,719,503	\$ 1,465,329
Operating income (loss)				
Steel Processing	\$ 41,130	\$ 35,448	\$ 74,002	\$ 90,230
Pressure Cylinders	24,675	11,304	35,133	25,409
Engineered Cabs	(1,587)	(3,381)	(1,948)	(5,224)
Other	(12,159)	(327)	(12,903)	(2,473)
Total operating income	\$ 52,059	\$ 43,044	\$ 94,284	\$ 107,942
Impairment of goodwill and long-lived assets				
Steel Processing	\$ -	\$ -	\$ -	\$ -
Pressure Cylinders	964	-	964	-
Engineered Cabs	-	-	-	-
Other	7,325	-	7,325	-
Total impairment of goodwill and long-lived assets	\$ 8,289	\$ -	\$ 8,289	\$ -
Restructuring and other expense (income), net				
Steel Processing	\$ (10,335)	\$ 318	\$ (10,056)	\$ 1,284
Pressure Cylinders	488	1,963	2,365	2,109
Engineered Cabs	(82)	1,004	(78)	1,210
Other	235	(13)	379	(3)
Total restructuring and other expense (income), net	\$ (9,694)	\$ 3,272	\$ (7,390)	\$ 4,600

(in thousands)

	November 30, 2017	May 31, 2017
Total assets		
Steel Processing	\$ 882,710	\$ 882,863
Pressure Cylinders	1,200,361	766,611
Engineered Cabs	66,957	62,141
Other	421,685	613,729
Total assets	\$ 2,571,713	\$ 2,325,344

Effective June 1, 2017, we made certain organizational changes impacting the internal reporting and management structure of Packaging Solutions. As a result of these organizational changes, management responsibilities and internal reporting were realigned, moving Packaging Solutions from the Steel Processing operating segment to the Engineered Cabs operating segment. Previously reported results have not been restated and are immaterial for all periods presented.

Table of Contents**NOTE N Acquisitions**

On June 2, 2017, the Company acquired Amtrol, a leading manufacturer of pressure cylinders and water system tanks with operations in the U.S. and Europe. The total purchase price was \$291,921,000 after adjusting for excess working capital and was funded primarily with cash on hand. The net assets became part of the Pressure Cylinders operating segment at closing, with the well water and expansion tank operations aligning under the consumer products business and the refrigerant, liquid propane and industrial and specialty gas operations aligning under the industrial products business. Total acquisition-related expenses were \$3,568,000, of which \$1,568,000 were incurred during fiscal 2018.

The information included herein has been prepared based on the preliminary allocation of the purchase price using estimates of the fair value and useful lives of the assets acquired and liabilities assumed. The purchase price allocation is subject to further adjustment until all pertinent information regarding the assets acquired and liabilities assumed are fully evaluated by the Company, including but not limited to, the fair value accounting, legal and tax matters, obligations, and deferred taxes.

The assets acquired and liabilities assumed were recognized at their preliminary acquisition-date fair values, with goodwill representing the excess of the purchase price over the fair value of the net identifiable assets acquired. In connection with the acquisition, we identified and valued the following identifiable intangible assets:

(in thousands)	Amount	Useful (Years)
<u>Category</u>		
Customer relationships	\$ 90,800	14-17
Trade names	62,200	Indefinite
Technology	13,000	15-16
Total acquired identifiable intangible assets	\$ 166,000	

The purchase price includes the fair values of other assets that were not identifiable, not separately recognizable under accounting rules (e.g., assembled workforce) or of immaterial value. The purchase price also includes a going-concern element that represents our ability to earn a higher rate of return on this group of assets than would be expected on the separate assets as determined during the valuation process. This additional investment value resulted in goodwill, which is not expected to be deductible for income tax purposes.

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The following table summarizes the consideration transferred for the assets of Amtrol and the preliminary fair value assigned to the assets acquired and liabilities assumed at the acquisition date:

(in thousands)	Preliminary	Measurement Period Adjustments	Revised Valuation
Cash	\$ 6,893	\$ -	\$ 6,893
Accounts receivable	40,212	-	40,212
Inventories	37,249	-	37,249
Prepaid expenses	981	-	981
Other assets	2,550	-	2,550
Intangible assets	166,000	-	166,000
Property, plant and equipment	52,870	-	52,870
Total assets	306,755	-	306,755
Accounts payable	25,945	-	25,945
Accrued liabilities	21,016	-	21,016
Long-term debt including current maturities	2,287	-	2,287
Other accrued items	3,993	-	3,993
Deferred income taxes, net	64,495	(413)	64,082
Net identifiable assets	189,019	413	189,432
Goodwill	102,902	(413)	102,489
Purchase price	\$ 291,921	\$ -	\$ 291,921
Less: excess working capital	(523)	-	(523)
Cash paid at closing	\$ 291,398	\$ -	\$ 291,398

Operating results of Amtrol have been included in the Company's consolidated statements of earnings since the date of the acquisition. During the three and six months ended November 30, 2017, Amtrol contributed net sales of \$67,935,000 and \$125,281,000, and operating income of \$6,441,000 and \$3,830,000, respectively.

The following unaudited pro forma information presents consolidated financial information as if Amtrol had been acquired at the beginning of fiscal 2017. Depreciation and amortization expense included in the pro forma results reflect the preliminary acquisition-date fair values assigned to the definite-lived intangible assets and fixed assets of Amtrol assuming a June 1, 2016 acquisition date. Adjustment has also been made for acquisition-related costs incurred in each period presented. Pro forma results for the three and six months ended November 30, 2017, have also been adjusted to remove the impact of the acquisition-date fair value adjustments to inventories and accrued severance costs related to headcount reductions at Amtrol initiated during fiscal 2018, as discussed in NOTE D Restructuring and Other Expense. The pro forma adjustments noted above have been adjusted for the applicable income tax impact. The pro forma information is presented for informational purposes only and is not indicative of the results of operations that would have been achieved if the acquisition had taken as of June 1, 2016.

(in thousands, except per share amounts)	Three months ended		Six months ended	
	November 30,		November 30,	
	2017	2016	2017	2016
Net sales	\$ 871,266	\$ 791,652	\$ 1,719,503	\$ 1,587,196
Net earnings attributable to controlling interest	\$ 39,711	\$ 47,469	\$ 89,182	\$ 117,826
Diluted earnings per share attributable to controlling interest	\$ 0.63	\$ 0.73	\$ 1.39	\$ 1.82

NOTE O Derivative Instruments and Hedging Activities

We utilize derivative financial instruments to manage exposure to certain risks related to our ongoing operations. The primary risks managed through the use of derivative instruments include interest rate risk, foreign currency exchange rate risk and commodity price risk. While certain of our derivative instruments are designated as hedging instruments, we also enter into derivative instruments that are designed to hedge a risk, but are not designated as hedging instruments and therefore do not qualify for hedge accounting. These derivative instruments are adjusted to current fair value through earnings at the end of each period.

Interest Rate Risk Management We are exposed to the impact of interest rate changes. Our objective is to manage the impact of interest rate changes on cash flows and the market value of our borrowings. We utilize a mix of debt maturities along with both fixed-rate and variable-rate debt to manage changes in interest rates. In addition, we enter into interest rate swaps and treasury locks to further manage our exposure to interest rate variations related to our borrowings and to lower our overall borrowing costs.

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Foreign Currency Exchange Risk Management We conduct business in several major international currencies and are therefore subject to risks associated with changing foreign currency exchange rates. We enter into various contracts that change in value as foreign currency exchange rates change to manage this exposure. Such contracts limit exposure to both favorable and unfavorable currency exchange rate fluctuations. The translation of foreign currencies into United States dollars also subjects us to exposure related to fluctuating currency exchange rates; however, derivative instruments are not used to manage this risk.

Commodity Price Risk Management We are exposed to changes in the price of certain commodities, including steel, natural gas, zinc and other raw materials, and our utility requirements. Our objective is to reduce earnings and cash flow volatility associated with forecasted purchases and sales of these commodities to allow management to focus its attention on business operations. Accordingly, we enter into derivative contracts to manage the associated price risk.

We are exposed to counterparty credit risk on all of our derivative instruments. Accordingly, we have established and maintain strict counterparty credit guidelines. We have credit support agreements in place with certain counterparties to limit our credit exposure. These agreements require either party to post cash collateral if its cumulative market position exceeds a predefined liability threshold. Amounts posted to the margin accounts accrue interest at market rates and are required to be refunded in the period in which the cumulative market position falls below the required threshold. We do not have significant exposure to any one counterparty, and management believes the risk of loss is remote and, in any event, would not be material.

Refer to NOTE P Fair Value for additional information regarding the accounting treatment for our derivative instruments, as well as how fair value is determined.

The following table summarizes the fair value of our derivative instruments and the respective line in which they were recorded in the consolidated balance sheet at November 30, 2017:

(in thousands)	Asset Derivatives		Liability Derivatives	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments:				
Commodity contracts	Receivables	\$ 3,721	Accounts payable	\$ -
	Other assets	649	Other liabilities	-
		4,370		-
Interest rate contracts	Receivables	-	Accounts payable	240
	Other assets	-	Other liabilities	25
		-		265
Totals		\$ 4,370		\$ 265
Derivatives not designated as hedging instruments:				
Commodity contracts	Receivables	\$ 1,692	Accounts payable	\$ 320
	Other assets	18	Other liabilities	-

		1,710		320
Foreign exchange contracts	Receivables	-	Accounts payable	46
Totals		\$ 1,710		\$ 366
Total derivative instruments		\$ 6,080		\$ 631

The amounts in the table above reflect the fair value of the Company's derivative contracts on a net basis. Had these amounts been recognized on a gross basis, the impact would have been a \$292,000 increase in receivables with a corresponding increase in accounts payable.

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The following table summarizes the fair value of our derivative instruments and the respective line in which they were recorded in the consolidated balance sheet at May 31, 2017:

(in thousands)	Asset Derivatives		Liability Derivatives	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments:				
Commodity contracts	Receivables	\$ 7,148	Accounts payable	\$ 111
	Other assets	6	Other liabilities	159
		7,154		270
Interest rate contracts	Receivables	-	Accounts payable	141
	Other assets	-	Other liabilities	160
		-		301
Totals		\$ 7,154		\$ 571
Derivatives not designated as hedging instruments:				
Commodity contracts	Receivables	\$ 1,110	Accounts payable	\$ 570
	Other assets	-	Other liabilities	1
		1,110		571
Foreign exchange contracts	Receivables	62	Accounts payable	-
Totals		\$ 1,172		\$ 571
Total derivative instruments		\$ 8,326		\$ 1,142

The amounts in the table above reflect the fair value of the Company's derivative contracts on a net basis. Had these amounts been recognized on a gross basis, the impact would have been a \$100,000 increase in receivables with a corresponding increase in accounts payable.

Cash Flow Hedges

We enter into derivative instruments to hedge our exposure to changes in cash flows attributable to interest rate and commodity price fluctuations associated with certain forecasted transactions. These derivative instruments are designated and qualify as cash flow hedges. Accordingly, the effective portion of the gain or loss on the derivative instrument is reported as a component of accumulated OCI and reclassified into earnings in the same line associated with the forecasted transaction and in the same period during which the hedged transaction affects earnings. The ineffective portion of the gain or loss on the derivative instrument is recognized in earnings immediately.

The following table summarizes our cash flow hedges outstanding at November 30, 2017:

(in thousands)	Notional Amount	Maturity Date
Commodity contracts	\$ 22,011	December 2017 - June 2019
Interest rate contracts	18,212	September 2019

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The following table summarizes the gain (loss) recognized in OCI and the gain (loss) reclassified from AOCI into earnings for derivative instruments designated as cash flow hedges during the three months ended November 30, 2017 and 2016:

(in thousands)	Gain Recognized in OCI (Effective Portion)	Location of Gain (Loss) Reclassified from Accumulated OCI (Effective Portion)	Gain (Loss) Reclassified from Accumulated OCI (Effective Portion)	Location of Gain (Ineffective Portion) and Excluded from Effectiveness Testing	Gain (Ineffective Portion) and Excluded from Effectiveness Testing
For the three months ended November 30, 2017:					
Commodity contracts	\$ 2,080	Cost of goods sold	\$ 5,637	Cost of goods sold	\$ -
Interest rate contracts	34	Interest expense	(28)	Interest expense	-
Totals	\$ 2,114		\$ 5,609		\$ -
For the three months ended November 30, 2016:					
Commodity contracts	\$ 7,157	Cost of goods sold	\$ 5,737	Cost of goods sold	\$ -
Interest rate contracts	160	Interest expense	(467)	Interest expense	-
Totals	\$ 7,317		\$ 5,270		\$ -

The following table summarizes the gain recognized in OCI and the gain reclassified from accumulated OCI into earnings for derivative instruments designated as cash flow hedges during the six months ended November 30, 2017 and 2016:

(in thousands)	Gain Recognized in OCI (Effective Portion)	Location of Gain (Loss) Reclassified from Accumulated OCI (Effective Portion)	Gain (Loss) Reclassified from Accumulated OCI (Effective Portion)	Location of Gain (Ineffective Portion) and Excluded from Effectiveness Testing	Gain (Ineffective Portion) and Excluded from Effectiveness Testing
For the six months ended November 30, 2017:					
Commodity contracts	\$ 5,814	Cost of goods sold	\$ 9,805	Cost of goods sold	\$ -
Interest rate contracts	3,098	Interest expense	(391)	Interest expense	-

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Totals	\$ 8,912		\$ 9,414		\$ -
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For the six months ended
November 30, 2016:

Commodity contracts	\$ 7,926	Cost of goods sold	\$ 5,485	Cost of goods sold	\$ -
Interest rate contracts	124	Interest expense	(570)	Interest expense	-

Totals	\$ 8,050		\$ 4,915		\$ -
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The estimated net amount of the losses recognized in AOCI at November 30, 2017 expected to be reclassified into net earnings within the succeeding twelve months is \$3,201,000 (net of tax of \$1,970,000). This amount was computed using the fair value of the cash flow hedges at November 30, 2017, and will change before actual reclassification from other comprehensive income to net earnings during the fiscal years ending May 31, 2018 and May 31, 2019.

Table of Contents**Economic (Non-designated) Hedges**

We enter into foreign currency contracts to manage our foreign exchange exposure related to inter-company and financing transactions that do not meet the requirements for hedge accounting treatment. We also enter into certain commodity contracts that do not qualify for hedge accounting treatment. Accordingly, these derivative instruments are adjusted to current market value at the end of each period through earnings.

The following table summarizes our economic (non-designated) derivative instruments outstanding at November 30, 2017:

(in thousands)	Notional Amount	Maturity Date(s)
Commodity contracts	\$ 25,427	December 2017 - May 2019
Foreign exchange contracts	5,469	December 2017 - June 2018

The following table summarizes the gain (loss) recognized in earnings for economic (non-designated) derivative financial instruments during the three months ended November 30, 2017 and 2016:

(in thousands)	Location of Gain (Loss) Recognized in Earnings	Gain (Loss) Recognized In Earnings for the Three Months Ended November 30,	
		2017	2016
Commodity contracts	Cost of goods sold	\$ (86)	\$ 2,003
Foreign exchange contracts	Miscellaneous income, net	19	(599)
Total		\$ (67)	\$ 1,404

The following table summarizes the gain recognized in earnings for economic (non-designated) derivative financial instruments during the six months ended November 30, 2017 and 2016:

(in thousands)	Location of Gain (Loss) Recognized in Earnings	Gain (Loss) Recognized in Earnings for the Six Months Ended November 30,	
		2017	2016
Commodity contracts	Cost of goods sold	\$ 2,248	\$ 4,911
Foreign exchange contracts	Miscellaneous income, net	(189)	(665)
Total		\$ 2,059	\$ 4,246

The gain (loss) on the foreign currency exchange contracts derivatives significantly offsets the gain (loss) on the hedged item.

Table of Contents**NOTE P Fair Value**

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is an exit price concept that assumes an orderly transaction between willing market participants and is required to be based on assumptions that market participants would use in pricing an asset or a liability. Current accounting guidance establishes a three-tier fair value hierarchy as a basis for considering such assumptions and for classifying the inputs used in the valuation methodologies. This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair values are as follows:

- Level 1 Observable prices in active markets for identical assets and liabilities.
- Level 2 Inputs other than quoted prices included within Level 1 that are observable for the assets and liabilities, either directly or indirectly.
- Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets and liabilities.

Recurring Fair Value Measurements

At November 30, 2017, our assets and liabilities measured at fair value on a recurring basis were as follows:

(in thousands)	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Totals
<u>Assets</u>				
Derivative contracts (1)	\$ -	\$ 6,080	\$ -	\$ 6,080
Total assets	\$ -	\$ 6,080	\$ -	\$ 6,080
<u>Liabilities</u>				
Derivative contracts (1)	\$ -	\$ 631	\$ -	\$ 631
Contingent consideration obligation (2)	-	-	601	601
Total liabilities	\$ -	\$ 631	\$ 601	\$ 1,232

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At May 31, 2017, our assets and liabilities measured at fair value on a recurring basis were as follows:

(in thousands)	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Totals
Assets				
Derivative contracts (1)	\$ -	\$ 8,326	\$ -	\$ 8,326
Total assets	\$ -	\$ 8,326	\$ -	\$ 8,326
Liabilities				
Derivative contracts (1)	\$ -	\$ 1,142	\$ -	\$ 1,142
Contingent consideration obligation (2)	-	-	585	585
Total liabilities	\$ -	\$ 1,142	\$ 585	\$ 1,727

(1) The fair value of our derivative instruments is based on the present value of the expected future cash flows considering the risks involved, including non-performance risk, and using discount rates appropriate for the respective maturities. Market observable, Level 2 inputs are used to determine the present value of the expected future cash flows. Refer to NOTE O Derivative Instruments and Hedging Activities for additional information regarding our use of derivative instruments.

(2) The fair value of the contingent consideration obligation is determined using a probability weighted cash flow approach based on management's projections of future cash flows of the acquired business. The fair value measurement was based on Level 3 inputs not observable in the market.

Non-Recurring Fair Value Measurements

At November 30, 2017, our assets measured at fair value on a non-recurring basis were as follows:

(in thousands)	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Totals
Assets				
Long-lived assets held and used (1)	\$ -	\$ 100	\$ -	\$ 100
Total assets	\$ -	\$ 100	\$ -	\$ 100

(1) During the second quarter of fiscal 2018, the Company determined that indicators of impairment were present with regard to the goodwill and intangible assets of the WEI reporting unit. As a result, these assets were written down to their estimated fair value of \$0 resulting in an impairment charge of \$7,325,000. The key assumptions that drove the fair value calculation were projected cash flows and the discount rate.

During the second quarter of fiscal 2018, the Company also identified impairment indicators to be present with regard to vacant land at the oil & gas equipment facility in Bremen, Ohio, resulting in an impairment charge of \$964,000 to write the land down to its estimated fair market value of \$100,000. Fair value was determined based on market prices for similar assets.

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At May 31, 2017, there were no assets or liabilities measured at fair value on a non-recurring basis on the Company's consolidated balance sheet.

The fair value of non-derivative financial instruments included in the carrying amounts of cash and cash equivalents, receivables, notes receivable, income taxes receivable, other assets, accounts payable, short-term borrowings, accrued compensation, contributions to employee benefit plans and related taxes, other accrued items, income taxes payable and other liabilities approximate carrying value due to their short-term nature. The fair value of long-term debt, including current maturities, based upon models utilizing market observable (Level 2) inputs and credit risk, was \$821,808,000 and \$618,059,000 at November 30, 2017 and May 31, 2017, respectively. The carrying amount of long-term debt, including current maturities, was \$779,930,000 and \$578,487,000 at November 30, 2017 and May 31, 2017, respectively.

NOTE Q Subsequent Events

On December 22, 2017, the Tax Cuts and Jobs Act (the "TCJA") was enacted into federal law. The TCJA includes significant changes to the U.S. corporate federal income tax system. Among other things, the TCJA lowers the corporate income tax rate to 21% from the current 35%, creates a territorial tax system (with a one-time mandatory tax on previously deferred foreign earnings), broadens the tax base and allows for immediate capital expensing of certain qualified property. While we are in the process of assessing the impact of the TCJA on future earnings, our best estimate of the Company's ongoing effective income tax rate as a result of the TCJA is 24% beginning in fiscal 2019. Results for the full fiscal year ending May 31, 2018 will reflect only five months of the lower federal income tax rate. In addition, the Company expects to record a non-cash tax benefit in the third quarter of fiscal 2018 to reflect the impact of the remeasurement of the Company's net deferred tax liability at the lower tax rate, currently estimated to be in the range of \$30,000,000 to \$40,000,000. The one-time mandatory tax on the Company's previously deferred foreign earnings is expected to be immaterial.

Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

Selected statements contained in this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations constitute forward-looking statements as that term is used in the Private Securities Litigation Reform Act of 1995. Such forward-looking statements are based, in whole or in part, on management's beliefs, estimates, assumptions and currently available information. For a more detailed discussion of what constitutes a forward-looking statement and of some of the factors that could cause actual results to differ materially from such forward-looking statements, please refer to the Safe Harbor Statement in the beginning of this Quarterly Report on Form 10-Q and Part I Item 1A. Risk Factors of our Annual Report on Form 10-K for the fiscal year ended May 31, 2017.

Introduction

The following discussion and analysis of market and industry trends, business developments, and the results of operations and financial position of Worthington Industries, Inc., together with its subsidiaries (collectively, we, our, Worthington, or the Company), should be read in conjunction with our consolidated financial statements and notes thereto included in Item 1. Financial Statements of this Quarterly Report on Form 10-Q. Our Annual Report on Form 10-K for the fiscal year ended May 31, 2017 (fiscal 2017) includes additional information about Worthington, our operations and our consolidated financial position and should be read in conjunction with this Quarterly Report on Form 10-Q.

As of November 30, 2017, excluding our joint ventures, we operated 34 manufacturing facilities worldwide, principally in three operating segments, which correspond with our reportable business segments: Steel Processing, Pressure Cylinders and Engineered Cabs. The Worthington Energy Innovations (WEI) operating segment does not meet the applicable aggregation criteria or quantitative thresholds for separate disclosure, and therefore is combined and reported in the Other category.

As of November 30, 2017, we held equity positions in 11 joint ventures, which operated 51 manufacturing facilities worldwide. Five of these joint ventures are consolidated with the equity owned by the other joint venture member(s) shown as noncontrolling interests in our consolidated balance sheets, and their portions of net earnings and other comprehensive income (loss) shown as net earnings or comprehensive income attributable to noncontrolling interests in our consolidated statements of earnings and consolidated statements of comprehensive income, respectively. The remaining six of these joint ventures are accounted for using the equity method.

Overview

The Company delivered overall sales growth of 20% for the second quarter of fiscal 2018 over the comparable period of fiscal 2017 on contributions from the June 2, 2017 acquisition of Amtrol, as discussed below under *Recent Business Developments*, higher overall volumes in Pressure Cylinders and higher average direct selling prices in Steel Processing. Pressure Cylinders reported record results on contributions from the Amtrol acquisition and strong demand in the legacy consumer and industrial products businesses. However, lower toll volumes in Steel Processing and lower contributions from our unconsolidated joint ventures led to a decline in net earnings from the prior year quarter.

Equity in net income of unconsolidated affiliates (equity income) decreased \$10.7 million from the prior year quarter due primarily to lower contributions from WAVE, ClarkDietrich and ArtiFlex. WAVE's contribution to equity income was \$5.0 million lower than the prior year quarter due primarily to an increase in allocated costs resulting from a new cost-sharing agreement between the joint venture and its partners, which required an adjustment of \$3.6 million to

equity income for the period covering January 1, 2017 to August 31, 2017. The Company's portion of allocated costs for the period covering the current quarter was approximately \$1.3 million, but this run rate is expected to decline by 40%-50% once the sale of WAVE's international business closes in calendar 2018, as discussed below under *Recent Business Developments*. The majority of the increase in allocated costs was from the joint venture partner and therefore is not offset elsewhere in the Company's results. ClarkDietrich's contribution to equity income was \$3.9 million lower than the prior year quarter as higher steel prices compressed margins. ArtiFlex's equity income was \$1.2 million below the prior year quarter due primarily to a decline in its offload business. We received distributions from unconsolidated joint ventures of \$19.4 million during the second quarter of fiscal 2018.

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Recent Business Developments

Effective June 1, 2017, we made certain organizational changes impacting the internal reporting and management structure of Packaging Solutions. As a result of these organizational changes, management responsibilities and internal reporting were realigned, moving Packaging Solutions from the Steel Processing operating segment to the Engineered Cabs operating segment. Previously reported results have not been restated and are immaterial for all periods presented.

On June 2, 2017, the Company acquired Amtrol, a leading manufacturer of pressure cylinders and water system tanks with operations in the U.S. and Europe. The total purchase price was \$291.9 million after adjusting for excess working capital and was funded primarily with cash on hand. The net assets became part of the Pressure Cylinders operating segment at closing, with the well water and expansion tank operations aligning under the consumer products business and the refrigerant, liquid propane and industrial and specialty gas operations aligning under the industrial products business. Refer to Item 1. Financial Statements Notes to Consolidated Financial Statements NOTE N Acquisitions.

On July 28, 2017, the Company completed the public offering of \$200.0 million aggregate principal amount of senior unsecured notes. The notes bear interest at a rate of 4.300% and mature on August 1, 2032. Refer to Item 1. Financial Statements Notes to Consolidated Financial Statements NOTE G Debt and Receivables Securitization.

On September 27, 2017, the Board of Directors of Worthington Industries, Inc. (the Board) authorized the repurchase of up to an additional 6,828,855 of the Company's common shares. During the second quarter of fiscal 2018, the Company repurchased a total of 1,500,000 common shares for \$67.4 million at an average price of \$44.97 per share, leaving 8,500,000 common shares available for repurchase.

On November 20, 2017, the Company announced that its unconsolidated joint venture, Worthington Armstrong Venture, a global leader in ceiling suspension systems solutions, has agreed to sell its business and operations in Europe, Middle East, Africa and Asia, to Knauf Group, a family-owned manufacturer of building materials headquartered in Germany. Worthington expects to receive proceeds of approximately \$45 million for its 50% share of the WAVE operations being sold. The transaction is subject to regulatory approvals and other customary closing conditions and is anticipated to close in the middle of calendar 2018.

On December 22, 2017, the Tax Cuts and Jobs Act was enacted into law, which among other things lowers the corporate federal income tax rate to 21% from the current 35%. Our best estimate of the Company's ongoing effective income tax rate as a result of the new legislation is 24% beginning in fiscal 2019. Results for the full fiscal year ending May 31, 2018 will reflect only five months of the lower rate. For additional information, refer to Item 1. Financial Statements Notes to Consolidated Financial Statements NOTE Q Subsequent Events.

On December 19, 2017, the Board declared a quarterly dividend of \$0.21 per share payable on March 29, 2018, to shareholders of record on March 15, 2018.

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Market & Industry Overview

We sell our products and services to a diverse customer base and a broad range of end markets. The breakdown of net sales by end market for the second quarter of each of fiscal 2018 and fiscal 2017 is illustrated in the following chart:

The automotive industry is one of the largest consumers of flat-rolled steel, and thus the largest end market for our Steel Processing operating segment. Approximately 61% of Steel Processing's net sales are to the automotive market. North American vehicle production, primarily by Ford, General Motors and FCA US (the Detroit Three automakers), has a considerable impact on the activity within this operating segment. The majority of the net sales of three of our unconsolidated joint ventures are also to the automotive market.

Approximately 13% of the net sales of our Steel Processing operating segment and 45% of the net sales of our Engineered Cabs operating segment are to the construction market. The construction market is also the predominant end market for two of our unconsolidated joint ventures: WAVE and ClarkDietrich. While the market price of steel significantly impacts these businesses, there are other key indicators that are meaningful in analyzing construction market demand, including U.S. gross domestic product (GDP), the Dodge Index of construction contracts and, in the case of ClarkDietrich, trends in the relative price of framing lumber and steel.

Substantially all of the net sales of our Pressure Cylinders operating segment, and approximately 26% and 55% of the net sales of our Steel Processing and Engineered Cabs operating segments, respectively, are to other markets such as consumer products, industrial, lawn and garden, agriculture, oil & gas equipment, heavy truck, mining, forestry and appliance. Given the many different products that make up these net sales and the wide variety of end markets, it is very difficult to detail the key market indicators that drive these portions of our business. However, we believe that the trend in U.S. GDP growth is a good economic indicator for analyzing these businesses.

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We use the following information to monitor costs and assess demand in our major end markets:

	Three Months Ended			Six Months Ended		
	November 30,			November 30,		
	2017	2016	Inc / (Dec)	2017	2016	Inc / (Dec)
U.S. GDP (% growth year-over-year) ¹	2.5%	1.5%	1.0%	2.2%	1.5%	0.7%
Hot-Rolled Steel (\$ per ton) ²	\$ 608	\$ 544	\$ 64	\$ 606	\$ 581	\$ 25
Detroit Three Auto Build (000 s vehicles) ³	2,128	2,380	(252)	4,207	4,710	(503)
No. America Auto Build (000 s vehicles) ³	4,328	4,758	(430)	8,465	9,407	(942)
Zinc (\$ per pound) ⁴	\$ 1.44	\$ 1.09	\$ 0.35	\$ 1.35	\$ 1.03	\$ 0.32
Natural Gas (\$ per mcf) ⁵	\$ 2.99	\$ 2.93	\$ 0.06	\$ 2.97	\$ 2.81	\$ 0.16
On-Highway Diesel Fuel Prices (\$ per gallon) ⁶	\$ 2.83	\$ 2.78	\$ 0.05	\$ 2.68	\$ 2.59	\$ 0.09
Crude Oil WTI (\$ per barrel) ⁶	\$ 52.68	\$ 46.89	\$ 5.79	\$ 49.67	\$ 46.47	\$ 3.20

¹ 2016 figures based on revised actuals ² CRU Hot-Rolled Index; period average ³ IHS Global ⁴ LME Zinc; period average ⁵ NYMEX Henry Hub Natural Gas; period average ⁶ Energy Information Administration; period average

U.S. GDP growth rate trends are generally indicative of the strength in demand and, in many cases, pricing for our products. A year-over-year increase in U.S. GDP growth rates is indicative of a stronger economy, which generally increases demand and pricing for our products. Conversely, decreasing U.S. GDP growth rates generally indicate a weaker economy. Changes in U.S. GDP growth rates can also signal changes in conversion costs related to production and in selling, general and administrative (SG&A) expense.

The market price of hot-rolled steel is one of the most significant factors impacting our selling prices and operating results. When steel prices fall, we typically have higher-priced material flowing through cost of goods sold, while selling prices compress to what the market will bear, negatively impacting our results. On the other hand, in a rising price environment, our results are generally favorably impacted, as lower-priced material purchased in previous periods flows through cost of goods sold, while our selling prices increase at a faster pace to cover current replacement costs.

The following table presents the average quarterly market price per ton of hot-rolled steel during fiscal 2018 (first and second quarters), fiscal 2017 and fiscal 2016:

	(Dollars per ton ¹)		
	Fiscal Year		
	2018	2017	2016
1st Quarter	\$ 604	\$ 617	\$ 461
2nd Quarter	\$ 608	\$ 544	\$ 419
3rd Quarter	N/A	\$ 608	\$ 381
4th Quarter	N/A	\$ 636	\$ 486

Annual Avg.	\$ 606	\$ 601	\$ 437
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¹ CRU Hot-Rolled Index, period average

No single customer contributed more than 10% of our consolidated net sales during the second quarter of fiscal 2018 or fiscal 2017. While our automotive business is largely driven by the production schedules of the Detroit Three automakers, our customer base is much broader and includes other domestic manufacturers and many of their suppliers. During the second quarter of fiscal 2018, vehicle production for the Detroit Three automakers was down 11%, while North American vehicle production as a whole was down 9%.

Certain other commodities, such as zinc, natural gas and diesel fuel, represent a significant portion of our cost of goods sold, both directly through our manufacturing operations and indirectly through transportation and freight expense.

Table of Contents**Results of Operations****Second Quarter Fiscal 2018 Compared to Fiscal 2017****Consolidated Operations**

The following table presents consolidated operating results for the periods indicated:

(In millions)	Three Months Ended November 30,				
	2017	% of Net sales	2016	% of Net sales	Increase/ (Decrease)
Net sales	\$ 871.3	100.0%	\$ 727.8	100.0%	\$ 143.5
Cost of goods sold	731.2	83.9%	605.0	83.1%	126.2
Gross margin	140.1	16.1%	122.8	16.9%	17.3
Selling, general and administrative expense	89.4	10.3%	76.5	10.5%	12.9
Impairment of goodwill and long-lived assets	8.3	1.0%	-	0.0%	8.3
Restructuring and other expense (income), net	(9.7)	-1.1%	3.3	0.5%	(13.0)
Operating income	52.1	6.0%	43.0	5.9%	9.1
Miscellaneous income, net	1.3	0.1%	0.9	0.1%	0.4
Interest expense	(10.0)	-1.1%	(7.6)	-1.0%	2.4
Equity in net income of unconsolidated affiliates (1)	16.4	1.9%	27.1	3.7%	(10.7)
Income tax expense	(18.2)	-2.1%	(13.5)	-1.9%	4.7
Net earnings	41.6	4.8%	49.9	6.9%	(8.3)
Net earnings attributable to noncontrolling interests	2.2	0.3%	3.3	0.5%	(1.1)
Net earnings attributable to controlling interest	\$ 39.4	4.5%	\$ 46.6	6.4%	\$ (7.2)
(1) Equity income by unconsolidated affiliate					
WAVE	\$ 13.7		\$ 18.7		\$ (5.0)
ClarkDietrich	0.4		4.3		(3.9)
Serviacero	1.5		2.0		(0.5)
ArtiFlex	0.9		2.1		(1.2)
Other	(0.1)		-		(0.1)
Total	\$ 16.4		\$ 27.1		\$ (10.7)

Net earnings attributable to controlling interest for the three months ended November 30, 2017 decreased \$7.2 million from the comparable period in the prior year. Net sales and operating highlights were as follows:

Net sales increased \$143.5 million over the comparable period in the prior year. The increase was driven by contributions from the acquisition of Amtrol, which totaled \$67.9 million, higher overall volumes in Pressure Cylinders and higher average selling prices in Steel Processing, partially offset by lower toll volumes. The balance of the increase was primarily the result of increased volume at Engineered Cabs.

Gross margin increased \$17.3 million over the comparable period in the prior year. The increase was driven by the contribution from the Amtrol acquisition and higher overall volumes in Pressure Cylinders, partially offset by lower direct spreads in Steel Processing.

SG&A expense increased \$12.9 million over the comparable period in the prior year. The increase was driven by the impact of the Amtrol acquisition, partially offset by lower profit sharing and bonus expense. Overall, SG&A expense was 10.3% of consolidated net sales compared to 10.5% in the comparable period of the prior year.

Impairment of goodwill and long-lived assets totaled \$8.3 million and consisted primarily of the impairment of goodwill and certain intangible assets at WEI. For additional information, refer to Item 1. Financial Statements Notes to Consolidated Financial Statements NOTE C Impairment of Goodwill and Long-Lived Assets.

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Restructuring and other income, net totaled \$9.7 million in the current period and resulted primarily from a net gain of \$10.6 million related to the sale of the legacy real estate of the Company's former stainless steel business, Precision Specialty Metals, Inc. (PSM). For additional information regarding the Company's restructuring activities, refer to Item 1. Financial Statements Notes to Consolidated Financial Statements NOTE D Restructuring and Other Expense.

Interest expense increased \$2.4 million over the comparable period in the prior year. The increase was primarily due to the issuance of \$200.0 million of aggregate principal amount senior unsecured notes due August 1, 2032. Refer to Item 1. Financial Statements Notes to Consolidated Financial Statements NOTE G Debt and Receivables Securitization.

Equity income decreased \$10.7 million from the comparable period in the prior year due primarily to lower contributions from WAVE, ClarkDietrich, and ArtiFlex. WAVE's contribution to equity income was \$5.0 million lower than the prior year quarter due primarily to an increase in allocated costs resulting from a new cost-sharing agreement between the joint venture and its partners, which required an adjustment of \$3.6 million to equity income for the period covering January 1, 2017 to August 31, 2017. ClarkDietrich's contribution to equity income was \$3.9 million lower than the prior year quarter as higher steel prices compressed margins. ArtiFlex's equity income was \$1.2 million below the prior year quarter due primarily to a decline in its offload business. We received distributions of \$19.4 million from our unconsolidated affiliates during the quarter. For additional information regarding our unconsolidated affiliates, refer to Item 1. Financial Statements Notes to Consolidated Financial Statements NOTE B Investments in Unconsolidated Affiliates.

Income tax expense increased \$4.7 million over the comparable period in the prior year due primarily to the impact of discrete items, offset partially by lower earnings. The current quarter expense was calculated using an estimated annual effective income tax rate of 30.0% versus 28.5% in the prior year quarter. Discrete items in the current quarter reduced income tax expense by \$0.6 million. Discrete items in the prior year quarter reduced income tax expense by \$6.4 million. Refer to Item 1. Financial Statements Notes to Consolidated Financial Statements NOTE K Income Taxes for more information on our tax rates.

Table of Contents**Segment Operations****Steel Processing**

The following table presents a summary of operating results for our Steel Processing operating segment for the periods indicated:

(Dollars in millions)	Three Months Ended November 30,				
	2017	% of Net sales	2016	% of Net sales	Increase/ (Decrease)
Net sales	\$ 538.4	100.0%	\$ 508.8	100.0%	\$ 29.6
Cost of goods sold	474.1	88.1%	437.2	85.9%	36.9
Gross margin	64.3	11.9%	71.6	14.1%	(7.3)
Selling, general and administrative expense	33.6	6.2%	35.8	7.0%	(2.2)
Restructuring and other expense (income), net	(10.4)	-1.9%	0.3	0.1%	(10.7)
Operating income	\$ 41.1	7.6%	\$ 35.5	7.0%	\$ 5.6
Material cost	\$ 380.3		\$ 339.0		\$ 41.3
Tons shipped (in thousands)	922		1,021		(99)

Net sales and operating highlights were as follows:

Net sales increased \$29.6 million over the comparable period in the prior year driven by higher average direct selling prices, which increased net sales by \$22.8 million, and higher direct volume, partially offset by lower toll volume due to declines at certain consolidated joint ventures. The mix of direct versus toll tons processed was 57% to 43% compared to 49% to 51% in the prior year quarter.

Operating income increased \$5.6 million over the comparable period in the prior year driven by a net gain of \$10.6 million related to the sale of the legacy real estate of the Company's former stainless steel business, PSM, partially offset by lower direct spreads and lower toll volume. Inventory holding gains were negligible in both the current and prior year quarters.

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Pressure Cylinders

The following table presents a summary of operating results for our Pressure Cylinders operating segment for the periods indicated: