

FRIEDMAN INDUSTRIES INC

Form 10-Q

November 14, 2007

**Table of Contents**

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**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2007

OR

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

COMMISSION FILE NUMBER 1-7521

**FRIEDMAN INDUSTRIES, INCORPORATED**

(Exact name of registrant as specified in its charter)

TEXAS  
(State or other jurisdiction of  
incorporation or organization)

74-1504405  
(I.R.S. Employer Identification  
Number)

4001 HOMESTEAD ROAD, HOUSTON, TEXAS 77028-5585  
(Address of principal executive office) (zip code)  
Registrant's telephone number, including area code (713) 672-9433

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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, and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer (  ) Accelerated filer (  ) Non-accelerated filer (  )

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

Yes  No

At September 30, 2007, the number of shares outstanding of the issuer's only class of stock was 6,712,108 shares of Common Stock.

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**TABLE OF CONTENTS**

**PART I FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**CONDENSED CONSOLIDATED BALANCE SHEETS UNAUDITED**

**CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS UNAUDITED**

**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS UNAUDITED**

**CONDENSED NOTES TO QUARTERLY REPORT UNAUDITED**

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

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

**Item 4. Controls and Procedures**

**Part II OTHER INFORMATION**

**Item 1. Legal Proceedings**

**Item 1A. Risk Factors**

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

**Item 3. Defaults Upon Senior Securities**

**Item 4. Submission of Matters to a Vote of Security Holders**

**Item 5. Other Information**

**Item 6. Exhibits**

**SIGNATURES**

**EXHIBIT INDEX**

**Certification Pursuant to Section 302 - William E. Crow**

**Certification Pursuant to Section 302 - Ben Harper**

**Certification Pursuant to Section 906 - William E. Crow**

**Certification Pursuant to Section 906 - Ben Harper**

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**Table of Contents****Part I FINANCIAL INFORMATION****Item 1. Financial Statements**

## FRIEDMAN INDUSTRIES, INCORPORATED

**CONDENSED CONSOLIDATED BALANCE SHEETS**

(Unaudited)

|  | SEPTEMBER 30, 2007                           | MARCH 31, 2007       |
|--|--|----------------------|
| <b>ASSETS</b>  |  |                      |
| <b>CURRENT ASSETS:</b>   |  |                      |
| Cash and cash equivalents  | \$ 4,026,604                                 | \$ 1,039,030         |
| Accounts receivable, net of allowances for bad debts and cash discounts of \$37,276 at September 30 and March 31, 2007 | 12,904,857                                   | 17,261,553           |
| Inventories  | 22,159,736                                   | 33,272,823           |
| Prepaid income taxes   | 477,628                                      |                      |
| Other  | 317,025                                      | 157,963              |
|  | <u>39,885,850</u>                            | <u>51,731,369</u>    |
| <b>PROPERTY, PLANT AND EQUIPMENT:</b>  |  |                      |
| Land   | 1,082,331                                    | 1,082,331            |
| Construction in progress   | 7,346,565                                    | 5,004,550            |
| Buildings and yard improvements  | 3,494,294                                    | 3,494,294            |
| Machinery and equipment  | 21,654,391                                   | 21,236,184           |
| Less accumulated depreciation  | (17,903,421)                                 | (17,344,822)         |
|  | <u>15,674,160</u>                            | <u>13,472,537</u>    |
| <b>OTHER ASSETS:</b>   |  |                      |
| Cash value of officers' life insurance and other assets  | 691,400                                      | 667,800              |
|  | <u>691,400</u>                               | <u>667,800</u>       |
| <b>TOTAL ASSETS</b>  | <b>\$ 56,251,410</b>                         | <b>\$ 65,871,706</b> |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>  |  |                      |
| <b>CURRENT LIABILITIES:</b>  |  |                      |
| Accounts payable and accrued expenses  | \$ 10,850,323                                | \$ 21,875,516        |
| Current portion of long-term debt  | 54,028                                       |                      |
| Dividends payable  | 536,969                                      | 536,969              |
| Income taxes payable   |  | 46,742               |
| Contribution to profit sharing plan  | 129,000                                      | 256,000              |
| Employee compensation and related expenses   | 488,770                                      | 551,356              |
|  | <u>12,059,090</u>                            | <u>23,266,583</u>    |
| <b>TOTAL CURRENT LIABILITIES</b>   | <b>12,059,090</b>                            | <b>23,266,583</b>    |
| <b>LONG-TERM DEBT LESS CURRENT PORTION</b>   | <b>94,549</b>                                |                      |
| <b>DEFERRED INCOME TAXES</b>   | <b>68,712</b>                                | <b>1,934</b>         |
| <b>POSTRETIREMENT BENEFITS OTHER THAN PENSIONS</b>   | <b>519,661</b>                               | <b>493,191</b>       |
| <b>STOCKHOLDERS' EQUITY:</b>   |  |                      |
| Common stock, par value \$1:   |  |                      |
| Authorized shares  | 10,000,000                                   |                      |
| Issued shares  | 7,887,824 at September 30 and March 31, 2007 | 7,887,824            |
| Additional paid-in capital   | 28,887,517                                   | 28,887,517           |
| Treasury stock at cost (1,175,716 shares at September 30 and March 31, 2007)   | (5,475,964)                                  | (5,475,964)          |

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|   |                             |                             |
|---|-----------------------------|-----------------------------|
| Retained earnings                         | 12,210,021                  | 10,810,621                  |
|   | <u>                    </u> | <u>                    </u> |
| TOTAL STOCKHOLDERS EQUITY                 | 43,509,398                  | 42,109,998                  |
|   | <u>                    </u> | <u>                    </u> |
| TOTAL LIABILITIES AND STOCKHOLDERS EQUITY | \$ 56,251,410               | \$ 65,871,706               |
|   | <u>                    </u> | <u>                    </u> |

**Table of Contents**

## FRIEDMAN INDUSTRIES, INCORPORATED

**CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS    UNAUDITED**

|   | Three months ended<br>September 30, |              | Six months ended<br>September 30, |               |
|---|-------------------------------------|--------------|-----------------------------------|---------------|
|   | 2007                                | 2006         | 2007                              | 2006          |
| Net sales                                 | \$41,154,571                        | \$51,629,944 | \$91,685,081                      | \$104,253,674 |
| Costs and expenses                        |                                     |              |                                   |               |
| Costs of goods sold                       | 38,722,209                          | 48,223,703   | 85,483,101                        | 95,970,757    |
| General, selling and administrative costs | 1,086,670                           | 1,306,226    | 2,506,163                         | 2,880,683     |
| Interest expense                          |                                     |              | 47,740                            |               |
| Gain on sale of assets                    |                                     | (1,312,839)  |                                   | (1,312,839)   |

**Table of Contents**

## FRIEDMAN INDUSTRIES, INCORPORATED

**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS UNAUDITED**

|   | Six Months Ended<br>September 30 |                     |
|---|----------------------------------|---------------------|
|   | 2007                             | 2006                |
| <b>OPERATING ACTIVITIES</b>   |                                  |                     |
| Net earnings  | \$ 2,473,337                     | \$ 4,413,004        |
| Adjustments to reconcile net income to cash provided by operating activities: |                                  |                     |
| Depreciation  | 558,601                          | 475,201             |
| Provision (benefit) for deferred taxes  | 66,778                           | 122,309             |
| Provision for postretirement benefits   | 26,470                           | 23,724              |
| Gain on sale of assets  |                                  | (1,312,839)         |
| Decrease (increase) in operating assets:                                      |                                  |                     |
| Accounts receivable   | 4,356,696                        | (727,141)           |
| Prepaid income taxes  | (477,628)                        |                     |
| Inventories   | 11,113,087                       | 1,061,119           |
| Other   | (159,062)                        | (260,690)           |
| Increase (decrease) in operating liabilities:                                 |                                  |                     |
| Accounts payable and accrued expenses   | (11,025,193)                     | 878,588             |
| Contribution to profit-sharing plan payable                                   | (127,000)                        | (121,000)           |
| Employee compensation and related expenses                                    | (62,586)                         | 53,974              |
| Income taxes payable  | (46,742)                         | (143,196)           |
| Deferred credit for LIFO replacement  |                                  | 271,403             |
| <b>NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES</b>                       | <b>6,696,758</b>                 | <b>4,734,456</b>    |
| <b>INVESTING ACTIVITIES</b>   |                                  |                     |
| Purchase of property, plant and equipment                                     | (2,760,223)                      | (2,935,538)         |
| (Increase) in cash surrender value of officers' life insurance                | (23,600)                         | (24,788)            |
| Proceeds from the sale of assets  |                                  | 1,388,318           |
| <b>NET CASH USED IN INVESTING ACTIVITIES</b>                                  | <b>(2,783,823)</b>               | <b>(1,572,008)</b>  |
| <b>FINANCING ACTIVITIES</b>   |                                  |                     |
| Cash dividends paid   | (1,073,938)                      | (1,066,660)         |
| Principal payments on notes payable   | (13,507)                         |                     |
| Tax benefit related to stock options  |                                  | 53,884              |
| Long-term debt  | 162,084                          |                     |
| <b>NET CASH PROVIDED (USED) IN FINANCING ACTIVITIES</b>                       | <b>(925,361)</b>                 | <b>(1,012,776)</b>  |
| <b>INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>                       | <b>2,987,574</b>                 | <b>2,149,672</b>    |
| Cash and cash equivalents at beginning of period                              | 1,039,030                        | 1,982,526           |
| <b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>                             | <b>\$ 4,026,604</b>              | <b>\$ 4,132,198</b> |

**Table of Contents**

## FRIEDMAN INDUSTRIES, INCORPORATED

**CONDENSED NOTES TO QUARTERLY REPORT    UNAUDITED**

## NOTE A    BASIS OF PRESENTATION

The accompanying unaudited condensed, consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. For further information, refer to the financial statements and footnotes included in the Company's annual report on Form 10-K for the year ended March 31, 2007.

## NOTE B    INVENTORIES

Inventories consist of prime coil, non-standard coil and tubular materials. Prime coil inventory consists primarily of raw materials, non-standard coil inventory consists primarily of finished goods and tubular inventory consists of both raw materials and finished goods. Inventories are valued at the lower of cost or replacement market. Cost for prime coil inventory is determined under the last-in, first-out ( LIFO ) method. Cost for non-standard coil inventory is determined using the specific identification method. Cost for tubular inventory is determined using the weighted average method.

During the period ended September 30, 2006, LIFO inventories were reduced but were replaced by March 31, 2007. A deferred credit of \$271,403 was recorded at September 30, 2006 to reflect replacement costs in excess of LIFO cost. LIFO inventories were also reduced in the period ended September 30, 2007 and are expected to be partially replaced by March 31, 2008. Since this replacement is not expected to have a significant impact on earnings, no deferred credit was recorded at September 30, 2007.

A summary of inventory values follows:

|                             | September 30,<br>2007 | March 31,<br>2007   |
|-----------------------------|-----------------------|---------------------|
| Prime Coil Inventory        | \$ 7,119,647          | \$ 11,034,422       |
| Non-Standard Coil Inventory | 723,270               | 665,234             |
| Tubular Raw Material        | 1,145,143             | 5,854,255           |
| Tubular Finished Goods      | 13,171,676            | 15,718,912          |
|                             | <u>\$22,159,736</u>   | <u>\$33,272,823</u> |

## NOTE C    LONG-TERM DEBT

The Company has a \$10 million revolving credit facility which expires April 1, 2010. There were no amounts outstanding pursuant to the facility at September 30, 2007 and March 31, 2007.

In June 2007, the Company incurred an interest free, long-term liability of \$162,084 related to the purchase of pipe loading equipment which is payable in 36 equal monthly payments.

## NOTE D    STOCK BASED COMPENSATION

Under the Company's 1989 and 1996 Stock Option Plans, options were granted to certain officers and key employees to purchase common stock of the Company. Pursuant to the terms of the plans, no additional options may be granted. All options have ten-year terms and become fully exercisable at the end of six months of continued employment. The following is a summary of activity relative to options outstanding during each of the quarters ended



September 30:

|   | 2007   |  | 2006    |  |
|---|--------|--|---------|--|
|   | Shares | Weighted<br>Average<br>Exercise<br>Price | Shares  | Weighted<br>Average<br>Exercise<br>Price |
| Outstanding at beginning of quarter                               | 88,836 | \$ 2.33                                  | 137,212 | \$ 2.35                                  |
| Granted   |        |  |         |  |
| Exercised   |        |  |         |  |
| Canceled or expired   |        |  | (2,894) | \$ 3.13                                  |
| Outstanding at end of quarter                                     | 88,836 | \$ 2.33                                  | 134,318 | \$ 2.33                                  |
| Exercisable at the end of the quarter                             | 88,836 | \$ 2.33                                  | 134,318 | \$ 2.33                                  |
| Weighted average fair value of options granted during the quarter |        |  |         |  |

The aggregate intrinsic value of exercisable and outstanding options at September 30, 2007 was \$579,211.

**Table of Contents**

## NOTE E SEGMENT INFORMATION

|                  | September 30,<br>2007 | March 31,<br>2007 |
|------------------|-----------------------|-------------------|
|                  | (in thousands)        | (in thousands)    |
| Segment assets   |                       |                   |
| Coil             | \$25,062              | \$27,601          |
| Tubular          | 25,936                | 36,491            |
|                  | 50,998                | 64,092            |
| Corporate assets | 5,253                 | 1,780             |
|                  | \$56,251              | \$65,872          |

Corporate expenses reflect general and administrative expenses not directly associated with segment operations and consist primarily of corporate executive and accounting salaries, professional fees and services, bad debts, accrued profit sharing expense, corporate insurance expenses and office supplies. Corporate assets consist primarily of cash and cash equivalents and the cash value of officers' life insurance.

## NOTE F SALE OF ASSETS

In September 2006, the Company closed on the sale of real property owned by the company in Houston, Texas. This sale resulted in a before tax gain of \$1,312,839. The proceeds from the sale of this property were used to purchase and improve real property associated with the new coil facility to be located in Decatur, Alabama.

## Note G RECENT ACCOUNTING PRONOUNCEMENT

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109 (FIN 48). This Interpretation provides guidance on recognition, classification and disclosure concerning uncertain tax liabilities. The evaluation of a tax position requires recognition of a tax benefit if it is more likely than not it will be sustained upon examination. We adopted this Interpretation effective January 1, 2007. The adoption did not have a material impact on our consolidated financial statements.

## Note H SUPPLEMENTAL CASH FLOW INFORMATION

The Company paid income taxes of approximately \$2,027,000 and \$2,690,000 in the periods ended September 30, 2007 and 2006, respectively. The Company paid interest of approximately \$48,000 and \$0 in the periods ended September 30, 2007 and 2006, respectively.

**Table of Contents**

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

**Results of Operations**

*Six Months Ended September 30, 2007 Compared to Six Months Ended September 30, 2006*

During the six months ended September 30, 2007, sales, costs of goods sold and gross profit decreased \$12,568,593, \$10,487,656 and \$2,080,937, respectively, from the comparable amounts recorded during the six months ended September 30, 2006. The decrease in sales was related to a decline in tons sold as well as a decrease in average selling prices. Tons shipped decreased from approximately 157,000 tons in the 2006 period to 145,000 tons in the 2007 period. The average per ton selling price decreased from approximately \$664 per ton in the 2006 period to approximately \$632 per ton in the 2007 period. The decline in costs of goods sold was primarily related to the decrease in sales. Average per ton costs of goods sold decreased from approximately \$611 per ton in the 2006 period to \$589 per ton in the 2007 period. The decrease in gross profit was related primarily to the reduction in tons shipped. In addition, gross profit as a percentage of sales decreased from approximately 7.9% in the 2006 period to 6.8% in the 2007 period. The Company experienced softer market conditions for its products in the 2007 period compared to strong market conditions in the 2006 period.

Coil product segment sales decreased approximately \$14,041,000 during the 2007 period. This segment experienced decreases in both tons sold and average selling prices. Tons of coil products sold declined from approximately 78,000 tons in the 2006 period to 61,000 tons in the 2007 period. Average per ton selling price decreased from approximately \$700 per ton to approximately \$662 per ton. Coil operating profit decreased approximately \$577,000 due primarily to the reduction in tons sold. Coil operating profit as a percentage of coil segment sales decreased from approximately 3.8% in the 2006 period to 3.6% in the 2007 period.

In the 2006 period, the Company phased out the Lone Star coil facility ( LSCF ). The LSCF accounted for approximately 1% of total sales and generated a small loss in the 2006 period. Certain LSCF assets will be redeployed to the Company's new coil operation to be located in Decatur, Alabama in close proximity to the Nucor Steel Company ( NSC ) steel mill located there. The Company expects to have this new facility in operation in fiscal 2008.

The Company is dependent on NSC for its supply of coil inventory. In the 2007 period, NSC continued to supply steel coils in amounts that were adequate for the Company's purposes. The Company does not currently anticipate any significant change in such supply from NSC.

Tubular product segment sales increased approximately \$1,472,000 during the 2007 period. This increase was primarily related to an increase in tons shipped in the 2007 period which was partially offset by a decline in average selling price. Tons shipped increased from approximately 79,000 tons in the 2006 period to 84,000 tons in the 2007 period. Average selling prices declined from approximately \$629 per ton in the 2006 period to \$609 per ton in the 2007 period. Tubular product segment operating profits as a percentage of segment sales were approximately 10.1% and 6.9% in the 2006 and 2007 periods, respectively. Margins were adversely affected by softer market conditions in the 2007 period.

Lone Star Steel Company ( LSS ) is the Company's primary supplier of tubular products and coil material used in pipe manufacturing. In June 2007, United States Steel Corporation consummated its purchase of LSS. In the 2007 period, LSS continued to supply the Company with pipe in amounts that were adequate for the Company's purposes.

LSS has also been one of the Company's principal customers for tubular products. A substantial portion of the coil material purchased from LSS is manufactured into tubular products and sold to LSS. Beginning in September 2007, the Company began to experience a decrease in the tons of pipe historically produced for LSS which resulted in a decrease in the Company's sales. The Company has been advised that this reduction is associated with the adjustment of inventory levels at LSS. If future production for LSS continues to be reduced, the Company believes that its sales will decline but gross profit will not be impacted proportionately as pipe produced for LSS is sold to LSS at a reduced profit margin.

During the 2007 period, general, selling and administrative costs decreased \$374,520 from the amount recorded during the 2006 period. This decrease was related primarily to decreases in commissions and bonuses associated with the decline in earnings and volume.

**Table of Contents**

In September 2006, the Company sold the real property owned by the Company in Houston, Texas and signed a twelve month rental agreement to rent corporate office space at this location for \$1,400 per month. This sale resulted in a before tax gain of \$1,312,839. Proceeds received from the sale were used to purchase and improve real property associated with the Company's new coil operation to be located in Decatur, Alabama.

Interest expense increased \$47,740 in the 2007 period. For two months in the 2007 period, the Company borrowed funds pursuant to its line of credit facility to support cash flow.

Interest and other income decreased \$26,483 from the comparable amount recorded in the 2006 period. This decrease was associated primarily with a decrease in the average invested cash positions in the 2007 period.

Income taxes decreased \$1,153,812 from the comparable amount recorded during the 2006 period. This decrease was primarily related to the decrease in earnings before taxes. Effective tax rates were 35.5% and 34.0% in the 2006 and 2007 periods, respectively. In the 2007 period, the Company benefited from a reduction in state taxes due to changes in state law and from a federal tax decrease associated with manufacturing companies.

*Three Months Ended September 30, 2007 Compared to Three Months Ended September 30, 2006*

During the three months ended September 30, 2007, sales, costs of goods sold and gross profit decreased \$10,475,373, \$9,501,494 and \$973,879, respectively, from the comparable amounts recorded during the three months ended September 30, 2006. The decrease in sales was related primarily to a decrease in tons sold which declined from approximately 76,000 tons in the 2006 quarter to 67,000 tons in the 2007 quarter. In addition, the average selling price per ton decreased from approximately \$682 per ton in the 2006 quarter to \$619 per ton in the 2007 quarter. The decrease in costs of goods sold was primarily related to the decrease in sales. The average per ton cost of goods decreased from approximately \$637 in the 2006 quarter to \$582 in the 2007 quarter. The reduction in gross profit was related to the reduction in tons sold and a decrease in margins. Gross profit as percentage of sales declined from approximately 6.6% in the 2006 quarter to approximately 5.9% in the 2007 quarter. The Company experienced softer market conditions for its products in the 2007 quarter compared to somewhat stronger market conditions in the 2006 quarter.

Coil product segment sales decreased approximately \$7,231,000 during the 2007 quarter. This decrease was related primarily to decrease in tons sold which decreased from approximately 37,000 tons in the 2006 quarter to 30,000 tons in the 2007 quarter. In addition, average selling prices decreased from approximately \$731 per ton in the 2006 quarter to \$648 per ton in the 2007 quarter. Coil operating profit increased approximately \$39,000 from the amount recorded in the 2006 quarter. Coil operating profits as a percentage of sales were approximately 1.9% and 2.8% in the 2006 and 2007 quarters, respectively. In the 2006 quarter, coil operations were adversely affected by an increase in cost of material that could not be passed along to customers in the short term.

Tubular product segment sales decreased approximately \$3,244,000 during the 2007 quarter. This decrease was related to a decrease in average per ton selling price and decline in tons sold. The average per ton selling price decreased from approximately \$636 per ton in the 2006 quarter to \$594 per ton in the 2007 quarter. In addition, tons sold decreased from approximately 39,000 tons in the 2006 quarter to 36,000 tons in the 2007 quarter. Tubular product segment operating profits as a percentage of segment sales were approximately 8.9% and 5.9% in the 2006 and 2007 quarters, respectively. The Company experienced somewhat softer market conditions for its pipe products in the 2007 quarter as compared to conditions in the 2006 quarter.

In June 2007, United States Steel Corporation consummated its purchase of LSS, one of the Company's principal customers for tubular products and the primary supplier of tubular products and coil material used in the Company's pipe manufacturing operations. A substantial portion of coil material purchased from LSS is manufactured into tubular products which are then sold to LSS. In the 2007 quarter, the Company began to experience a decrease in the tons of pipe historically produced for LSS which resulted in a decrease in the Company's sales of approximately \$1,300,000. The Company has been advised that this reduction is associated with the adjustment of inventory levels at LSS. If future production for LSS continues to be reduced, the Company believes that its sales will decline but gross profit will not be impacted proportionately as pipe produced for LSS is sold to LSS at a reduced profit margin.

General, selling and administrative costs declined \$219,556 from the amount recorded in the 2006 quarter. This decline was related primarily to bonuses and commissions based on earnings or volume.

In September 2006, the Company sold the real property owned by the Company in Houston, Texas and signed a twelve month rental agreement to rent corporate office space at this location for \$1,400 per month. This sale resulted in a before tax gain of \$1,312,839. Proceeds

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received from the sale were used to purchase and improve real property associated with the Company's new coil operation to be located in Decatur, Alabama.

Interest and other income decreased \$10,805 from the comparable amount recorded in the 2006 quarter. This decrease was associated primarily with a decrease in the average invested cash positions in the 2007 quarter.

Federal income taxes decreased \$730,990 from the comparable amount recorded during the 2006 quarter. This decrease was primarily related to the decrease in earnings before taxes. Effective tax rates were 34.8% and 34.3% in the 2006 and 2007 quarters, respectively.

**Table of Contents**

**FINANCIAL POSITION, LIQUIDITY AND CAPITAL RESOURCES**

The Company remained in a strong, liquid position at September 30, 2007. Current ratios were 3.3 and 2.2 at September 30, 2007 and March 31, 2007, respectively. Working capital was \$27,826,760 at September 30, 2007 and \$28,464,786 at March 31, 2007.

During the three months ended September 30, 2007, the Company maintained assets and liabilities at levels it believed were commensurate with operations. Changes in current assets and liabilities during the 2007 period were related primarily to the ordinary course of business of the Company. The Company expects to continue to monitor, evaluate and manage balance sheet components depending on changes in market conditions and the Company's operations.

During the period ended September 30, 2007, the Company purchased approximately \$2,760,223 in fixed assets. These assets were related primarily to equipment associated with the new coil operation to be located in Decatur, Alabama. In connection with this planned new operation, the Company phased out its coil processing facility in Lone Star, Texas in the 2006 period and will redeploy certain of these assets to this new coil facility. At the Decatur site, the Company is constructing a coil processing facility to include a steel temper mill and a steel cut-to-length line including a leveling line. The Company expects to commence operations at the Decatur site in fiscal 2008. In addition to the funds used to purchase the real property in Alabama, the Company's Board of Directors authorized up to an additional \$16 million to be used for capital expenditures and operational cash requirements at this location. At September 30, 2007, the Company had invested approximately \$8,800,000 at this location and expects to spend approximately \$700,000 to complete this facility.

The Company has an arrangement with a bank which provides for a revolving line of credit facility (the revolving facility). Pursuant to the revolving facility, which expires April 1, 2010, the Company may borrow up to \$10 million at the bank's prime rate or 1.5% over LIBOR. The Company uses the revolving facility to support cash flow and will borrow and repay the note as working capital is required. At September 30, 2007 and March 31, 2007, the Company had no borrowings outstanding under the revolving facility.

The Company has in the past and may in the future borrow funds on a term basis to build or improve facilities. The Company currently has no plans to borrow any significant amount of funds on a term basis.

Notwithstanding the current market conditions, the Company believes its cash flows from operations and borrowing capability under its revolving facility are adequate to fund its expected cash requirements for the next twenty-four months.

**CRITICAL ACCOUNTING POLICIES**

The preparation of consolidated financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. One such accounting policy which requires significant estimates and judgments is the valuation of LIFO inventories in the Company's quarterly reporting. The quarterly valuation of inventory requires estimates of the year end quantities which is inherently difficult. Historically, these estimates have been materially correct. In addition, the Company maintains an allowance for doubtful accounts receivable by providing for specifically identified accounts where collectibility is doubtful. On an ongoing basis, the Company evaluates estimates and judgments. The Company bases its estimates on historical experience and on various other assumptions that it believes to be reasonable under the circumstances.

**FORWARD-LOOKING STATEMENTS**

From time to time, the Company may make certain statements that contain forward-looking information (as defined in the Private Securities Litigation Reform Act of 1996) and that involve risk and uncertainty. These forward-looking statements may include, but are not limited to, future results of operations, future production capacity, product quality and proposed expansion plans. Forward-looking statements may be made by management orally or in writing including, but not limited to, this Management's Discussion and Analysis of Financial Condition and Results of Operations and other sections of the Company's filings with the Securities and Exchange Commission under the Securities Act of 1933 and the Securities Exchange Act of 1934. Actual results and trends in the future may differ materially depending on a variety of factors including but not limited to changes in the demand and prices of the Company products, changes in the demand for steel and steel products in general and the Company's success in executing its internal operating plans, including any proposed expansion plans.

**Table of Contents**

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

In the normal course of business the Company is exposed to market risks primarily from changes in the cost of steel in inventory and in interest rates. The Company closely monitors exposure to market risks and develops appropriate strategies to manage risk. With respect to steel purchases, there is no recognized market to purchase derivative financial instruments to reduce the inventory exposure risk on changing commodity prices. The exposure to market risk associated with interest rates relates primarily to debt. Recent debt balances are minimal and, as a result, direct exposure to interest rates changes is not significant.

**Item 4. Controls and Procedures**

The Company's management, with the participation of the Company's principal executive officer (CEO) and principal financial officer (CFO), evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the Exchange Act)), as of the end of the period ended September 30, 2007. Based on this evaluation, the CEO and CFO have concluded that the Company's disclosure controls and procedures were effective as of the end of the period September 30, 2007 to ensure that information that is required to be disclosed by the Company in the reports it files or submits under the Exchange Act is (i) recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms and (ii) accumulated and communicated to the Company's management, including the CEO and CFO, as appropriate, to allow timely decisions regarding required disclosure.

There were no changes in the Company's internal control over financial reporting that occurred during the period ended September 30, 2007 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**Table of Contents**

**FRIEDMAN INDUSTRIES, INCORPORATED**

**Three Months Ended September 30, 2007**

**Part II OTHER INFORMATION**

**Item 1. Legal Proceedings**

Not applicable

**Item 1A. Risk Factors**

Not applicable

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

a). Not applicable

b). Not applicable

c). Not applicable

**Item 3. Defaults Upon Senior Securities**

a). Not applicable

b). Not applicable

**Item 4. Submission of Matters to a Vote of Security Holders**

At the Annual Meeting of Shareholders held on September 6, 2007, the Company's shareholders elected nine directors to the Company's Board of Directors. The number of shares voted for and withheld with respect to the election of each director was as follows:

| <b>Name</b>     | <b>Shares Voted For</b> | <b>Shares Withheld</b> |
|-----------------|-------------------------|------------------------|
| Jack Friedman   | 4,290,222               | 1,593,772              |
| Harold Friedman | 4,295,144               | 1,588,850              |
| William E. Crow | 4,304,975               | 1,579,019              |
| Durga D. Arawal | 5,523,090               | 360,904                |
| Charles W. Hall | 4,053,564               | 1,830,430              |
| Alan M. Rauch   | 5,510,972               | 373,022                |
| Hershel M. Rich | 5,520,329               | 363,665                |
| Joel Spira      | 5,647,735               | 236,259                |
| Joe L. Williams | 4,291,312               | 1,592,682              |

**Item 5. Other Information**

Not applicable

**Item 6. Exhibits**



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Exhibits

- 31.1 Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, signed by William E. Crow
- 31.2 Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, signed by Ben Harper
- 32.1 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, signed by William E. Crow
- 32.2 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, signed by Ben Harper



**Table of Contents**

**EXHIBIT INDEX**

| <b>Exhibit No.</b> | <b>Description</b>  |
|--------------------|---|
| Exhibit 31.1       | Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, signed by William E. Crow  |
| Exhibit 31.2       | Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, signed by Ben Harper   |
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