

AMERICAN AXLE & MANUFACTURING HOLDINGS INC
Form 10-Q
July 29, 2011

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2011

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: 1-14303

AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.
(Exact Name of Registrant as Specified in Its Charter)

Delaware 38-3161171
(State or Other Jurisdiction of Incorporation or Organization) (I.R.S. Employer Identification No.)

One Dauch Drive, Detroit, Michigan 48211-1198
(Address of Principal Executive Offices) (Zip Code)
(313) 758-2000
(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes 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, or a smaller reporting company. See definition of "accelerated filer," "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

As of July 27, 2011, the latest practicable date, the number of shares of the registrant's Common Stock, par value \$0.01 per share, outstanding was 75,334,588 shares.

Internet Website Access to Reports

The website for American Axle & Manufacturing Holdings, Inc. is www.aam.com. Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13 or 15(d) of the Exchange Act are available free of charge through our website as soon as reasonably practicable after they are electronically filed with, or furnished to, the Securities and Exchange Commission (SEC). The SEC also maintains a website at www.sec.gov that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC.

AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.
 FORM 10-Q
 FOR THE QUARTER ENDED JUNE 30, 2011
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FORWARD-LOOKING STATEMENTS

In this Quarterly Report on Form 10-Q (Quarterly Report), we make statements concerning our expectations, beliefs, plans, objectives, goals, strategies, and future events or performance. Such statements are “forward-looking” statements within the meaning of the Private Securities Litigation Reform Act of 1995 and relate to trends and events that may affect our future financial position and operating results. The terms such as “will,” “may,” “could,” “would,” “plan,” “believe,” “expect,” “anticipate,” “intend,” “project,” and similar words of expressions, as well as statements in future tense, are intended to identify forward-looking statements.

Forward-looking statements should not be read as a guarantee of future performance or results, and will not necessarily be accurate indications of the times at, or by, which such performance or results will be achieved. Forward-looking statements are based on information available at the time those statements are made and/or management’s good faith belief as of that time with respect to future events and are subject to risks and may differ materially from those expressed in or suggested by the forward-looking statements. Important factors that could cause such differences include, but are not limited to:

- global economic conditions;
- our ability to comply with the definitive terms and conditions of various commercial and financing arrangements with General Motors Company (GM);
- reduced purchases of our products by GM, Chrysler Group LLC (Chrysler) or other customers;
- reduced demand for our customers’ products (particularly light trucks and sport utility vehicles (“SUVs”) produced by GM and Chrysler);
- availability of financing for working capital, capital expenditures, research and development (“R&D”) or other general corporate purposes, including our ability to comply with financial covenants;
- our customers’ and suppliers’ availability of financing for working capital, capital expenditures, R&D or other general corporate purposes;
- our ability to achieve cost reductions through ongoing restructuring actions;
- our ability to achieve the level of cost reductions required to sustain global cost competitiveness;
- our ability, our suppliers’ ability and our customers’ ability to avoid supply shortages as a result of recent events in Japan or otherwise;
- our ability to maintain satisfactory labor relations and avoid future work stoppages;
- our suppliers’, our customers’ and their suppliers’ ability to maintain satisfactory labor relations and avoid work stoppages;
- additional restructuring actions that may occur;
- our ability to continue to implement improvements in our U.S. labor cost structure;
- supply shortages or price increases in raw materials, utilities or other operating supplies;
- our ability to consummate and integrate acquisitions and joint ventures;
- our ability or our customers’ and suppliers’ ability to successfully launch new product programs on a timely basis;
- our ability to realize the expected revenues from our new and incremental business backlog;
- our ability to attract new customers and programs for new products;
- our ability to develop and produce new products that reflect market demand;
- lower-than-anticipated market acceptance of new or existing products;
- our ability to respond to changes in technology, increased competition or pricing pressures;
- price volatility in, or reduced availability of, fuel;
- adverse changes in laws, government regulations or market conditions affecting our products or our customers’ products (such as the Corporate Average Fuel Economy (“CAFE”) regulations);
- risks inherent in our international operations (including adverse changes in the political stability, taxes and other law changes, potential disruption of production and supply, and currency rate fluctuations);
-

liabilities arising from warranty claims, product recall, product liability and legal proceedings to which we are or may become a party;

• changes in liabilities arising from pension and other postretirement benefit obligations;

• risks of noncompliance with environmental regulations or risks of environmental issues that could result in unforeseen costs at our facilities;

• our ability to attract and retain key associates;

• other unanticipated events and conditions that may hinder our ability to compete.

It is not possible to foresee or identify all such factors and we make no commitment to update any forward-looking statement or to disclose any facts, events or circumstances after the date hereof that may affect the accuracy of any forward-looking statement.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended		Six Months Ended	
	June 30,	2010	June 30,	2010
	2011		2011	
	(in millions, except per share data)			
Net sales	\$686.2	\$559.6	\$1,331.8	\$1,081.5
Cost of goods sold	555.7	460.7	1,085.9	895.3
Gross profit	130.5	98.9	245.9	186.2
Selling, general and administrative expenses	58.8	48.5	115.5	93.8
Operating income	71.7	50.4	130.4	92.4
Interest expense	(20.5	) (22.6	) (41.8	) (45.3
Investment income	0.3	0.6	0.6	1.0
Other income (expense)				
Debt refinancing and redemption costs	(3.1	) —	(3.1) —
Other, net	(0.7	) (0.7	) 0.3	(2.2
Income before income taxes	47.7	27.7	86.4	45.9
Income tax expense (benefit)	(0.2	) 2.4	1.9	4.4
Net income	47.9	25.3	84.5	41.5
Net loss attributable to the noncontrolling interests	1.3	0.1	2.4	0.2
Net income attributable to AAM	\$49.2	\$25.4	\$86.9	\$41.7
Basic earnings per share	\$0.65	\$0.36	\$1.17	\$0.58
Diluted earnings per share	\$0.65	\$0.34	\$1.15	\$0.56

See accompanying notes to condensed consolidated financial statements.

AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

	June 30, 2011 (Unaudited) (in millions)	December 31, 2010
Assets		
Current assets		
Cash and cash equivalents	\$250.3	\$244.6
Accounts receivable, net	199.0	146.6
Inventories, net	148.5	130.3
Prepaid expenses and other current assets	80.8	80.6
Total current assets	678.6	602.1
Property, plant and equipment, net	960.4	936.3
Goodwill	156.6	155.8
GM postretirement cost sharing asset	240.5	244.4
Other assets and deferred charges	159.3	176.1
Total assets	\$2,195.4	\$2,114.7
Liabilities and Stockholders' Deficit		
Current liabilities		
Accounts payable	\$355.0	\$283.6
Accrued compensation and benefits	116.5	115.1
Deferred revenue	60.5	79.9
Accrued expenses and other current liabilities	96.5	90.5
Total current liabilities	628.5	569.1
Long-term debt	964.6	1,010.0
Deferred revenue	97.7	116.0
Postretirement benefits and other long-term liabilities	862.5	887.7
Total liabilities	2,553.3	2,582.8
Stockholders' deficit		
Common stock, par value \$0.01 per share	0.8	0.8
Paid-in capital	595.8	588.1
Accumulated deficit	(699.4)	(786.3)
Treasury stock at cost, 5.5 million shares as of June 30, 2011 and December 31, 2010	(176.2)	(176.1)
Accumulated other comprehensive income (loss), net of tax		
Defined benefit plans	(148.6)	(152.1)
Foreign currency translation adjustments	57.5	44.8
Unrecognized gain on derivatives	2.4	1.3
Total AAM stockholders' deficit	(367.7)	(479.5)
Noncontrolling interest in subsidiaries	9.8	11.4
Total stockholders' deficit	(357.9)	(468.1)
Total liabilities and stockholders' deficit	\$2,195.4	\$2,114.7

See accompanying notes to condensed consolidated financial statements.

AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (Unaudited)

	Six Months Ended June 30,	
	2011	2010
	(in millions)	
Operating activities		
Net income	\$84.5	\$41.5
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	68.8	64.4
Asset impairments and related indirect inventory obsolescence	—	8.7
Deferred income taxes	22.3	—
Stock-based compensation	3.1	4.9
Pensions and other postretirement benefits, net of contributions	1.6	(16.3)
Loss (gain) on disposal of property, plant and equipment, net	(6.5)	) 0.1
Debt refinancing and redemption costs	1.8	—
Changes in operating assets and liabilities		
Accounts receivable	(50.3)	) (43.0)
Inventories	(16.8)	) (26.6)
Accounts payable and accrued expenses	67.3	117.1
Deferred revenue	(37.7)	) (29.6)
Other assets and liabilities	(21.6)	) 43.7
Net cash provided by operating activities	116.5	164.9
Investing activities		
Purchases of property, plant and equipment	(71.6)	) (36.9)
Proceeds from sale of property, plant and equipment	7.8	1.2
Purchase buyouts of leased equipment	—	(7.4)
Redemption of short-term investments	—	1.6
Net cash used in investing activities	(63.8)	) (41.5)
Financing activities		
Net short-term borrowings (repayments) under revolving credit facilities	—	(60.0)
Payments of long-term debt and capital lease obligations	(49.2)	) (4.8)
Proceeds from issuance of long-term debt	1.8	7.3
Debt issuance costs	(5.3)	) (2.2)
Repurchase of treasury stock	(0.1)	) (1.3)
Employee stock option exercises	4.6	—
Net cash used in financing activities	(48.2)	) (61.0)
Effect of exchange rate changes on cash	1.2	(1.8)
Net increase in cash and cash equivalents	5.7	60.6
Cash and cash equivalents at beginning of period	244.6	178.1
Cash and cash equivalents at end of period	\$250.3	\$238.7

Supplemental cash flow information

Interest paid	\$38.2	\$20.3
Income taxes paid (refunds received), net	\$2.8	\$(45.1)

See accompanying notes to condensed consolidated financial statements.

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AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
 June 30, 2011
 (Unaudited)

1. ORGANIZATION AND BASIS OF PRESENTATION

Organization American Axle & Manufacturing Holdings, Inc. (Holdings) and its subsidiaries (collectively, we, our, us or AAM) is a Tier I supplier to the automotive industry. We manufacture, engineer, design and validate driveline and drivetrain systems and related components and chassis modules for light trucks, sport utility vehicles (SUVs), passenger cars, crossover vehicles and commercial vehicles. Driveline and drivetrain systems include components that transfer power from the transmission and deliver it to the drive wheels. Our driveline, drivetrain and related products include axles, chassis modules, driveshafts, power transfer units, transfer cases, chassis and steering components, driveheads, crankshafts, transmission parts and metal-formed products. In addition to locations in the United States (U.S.) (Michigan, New York, Ohio, Indiana and Pennsylvania), we also have offices or facilities in Brazil, China, Germany, India, Japan, Luxembourg, Mexico, Poland, Scotland, South Korea, Sweden and Thailand.

Basis of Presentation We have prepared the accompanying interim condensed consolidated financial statements in accordance with the instructions to Form 10-Q under the Securities Exchange Act of 1934. These condensed consolidated financial statements are unaudited but include all normal recurring adjustments, which we consider necessary for a fair presentation of the information set forth herein. Results of operations for the periods presented are not necessarily indicative of the results for the full fiscal year.

The balance sheet at December 31, 2010 presented herein has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States of America (GAAP) for complete consolidated financial statements.

In order to prepare the accompanying interim condensed consolidated financial statements, we are required to make estimates and assumptions that affect the reported amounts and disclosures in our interim condensed consolidated financial statements. Actual results could differ from those estimates.

For further information, refer to the audited consolidated financial statements and notes included in our Annual Report on Form 10-K for the year ended December 31, 2010.

2. RESTRUCTURING ACTIONS

A summary of the restructuring related activity for the six months ended June 30, 2011 is shown below (in millions):

	One-time Termination Benefits	Asset Retirement Obligations	Contract Related Costs	Total
Accrual as of December 31, 2010	\$1.2	\$1.4	\$12.2	\$14.8
Cash utilization	(0.4	) (0.1	) (3.5	) (4.0
Accrual adjustments	—	0.1	—	0.1
Accrual as of June 30, 2011	\$0.8	\$1.4	\$8.7	\$10.9

We expect to make payments of approximately \$6 million during the remainder of 2011 and \$5 million in 2012 related to the remaining restructuring accrual.

AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

3. INVENTORIES

We state our inventories at the lower of cost or market. The cost of worldwide inventories is determined using the FIFO method. When we determine that our gross inventories exceed usage requirements, or if inventories become obsolete or otherwise not saleable, we record a provision for such loss as a component of our inventory accounts.

Inventories consist of the following:

	June 30, 2011	December 31, 2010
	(in millions)	
Raw materials and work-in-progress	\$ 155.7	\$ 137.7
Finished goods	23.2	20.3
Gross inventories	178.9	158.0
Inventory valuation reserves	(30.4	) (27.7
Inventories, net	\$ 148.5	\$ 130.3

4. LONG-TERM DEBT

Long-term debt consists of the following:

	June 30, 2011	December 31, 2010
	(in millions)	
Amended and Restated Revolving Credit Facility	\$—	\$—
9.25% Notes, net of discount	378.7	420.3
7.875% Notes	300.0	300.0
5.25% Notes, net of discount	249.9	249.9
2.00% Convertible Notes	—	0.4
Foreign credit facilities	29.5	32.6
Capital lease obligations	6.5	6.8
Long-term debt	\$964.6	\$ 1,010.0

On June 6, 2011, we voluntarily redeemed 10% of our 9.25% Notes outstanding at a redemption price of 103% of the principal amount. This resulted in a principal payment of \$42.5 million and a \$1.3 million payment for the redemption premium, as well as a payment related to accrued interest. Upon repayment, we expensed \$1.4 million for the write off of a proportional amount of unamortized debt discount and issuance costs related to this debt. We had been amortizing the debt issuance costs and debt discount over the expected life of the borrowing.

On June 30, 2011, we amended and restated the Credit Agreement dated as of January 9, 2004 (as amended and restated, the “Amended and Restated Revolving Credit Agreement” and the facility thereunder, the “Amended Revolving Credit Facility”). As of June 30, 2011, the Revolving Credit Facility provided up to \$53.1 million of revolving bank financing commitments through December 2011, \$86.9 million of such revolving bank financing commitments through June 2013 and \$235.0 million of such revolving bank financing commitments through June 30, 2016. At June 30, 2011, we had \$345.0 million available under the Revolving Credit Facility. This availability reflects a reduction of \$30.0 million for standby letters of credit issued against the facility.

The Amended and Restated Revolving Credit Agreement, among other things, increased the aggregate commitments by approximately \$79.0 million and extended the maturity of \$235.0 million of the aggregate commitments to June 30, 2016. We paid debt issuance costs of \$5.3 million in the second quarter of 2011 associated with the amendments and restatements of our Revolving Credit Facility.

AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Borrowings under the Amended and Restated Revolving Credit Facility bear interest at rates based on adjusted LIBOR or an alternate base rate, plus an applicable margin. The applicable margin for LIBOR based loans for lenders who extended their maturities will be between 3.00% and 4.50%, depending upon the corporate ratings of the Company. The applicable margin for lenders who did not extend their maturities remains the same.

Under the Amended and Restated Revolving Credit Facility, we are required to comply with financial covenants related to secured indebtedness leverage, total net leverage, and cash interest expense coverage. The Amended and Restated Revolving Credit Facility limits our ability to make certain investments, declare or pay dividends or distributions on capital stock, redeem or repurchase capital stock and certain debt obligations, incur liens, incur indebtedness, or merge, make acquisitions and sell assets.

The Amended and Restated Revolving Credit Facility is secured on a first priority basis by substantially all of the assets of Holdings, AAM Inc. and each guarantor party thereto, including a pledge of all capital stock of the U.S. subsidiaries of Holdings and each guarantor and a portion of the capital stock of AAM Inc. and each guarantor's first-tier foreign subsidiaries. In addition, obligations under the Amended and Restated Revolving Credit Facility are guaranteed by Holdings and AAM Inc.'s U.S. subsidiaries, all of which are directly owned by AAM Inc.

The Amended and Restated Revolving Credit Facility provides back-up liquidity for our foreign credit facilities. We intend to use the availability of long-term financing under the Amended and Restated Revolving Credit Facility to refinance any current maturities related to such debt agreements that are not otherwise refinanced on a long-term basis in their local markets.

As part of the 2009 Settlement and Commercial Agreement with GM, we entered into certain agreements which, among other things, provided us with expedited payment terms of "net 10 days" in exchange for a 1% early payment discount and a Second Lien Term Loan Agreement through December 31, 2013. Pursuant to the terms of such agreements, we elected to terminate the expedited payment terms as well as the Second Lien Term Loan Agreement, effective June 30, 2011. As a result of these terminations, our Access and Security Agreement with GM is due to expire on September 28, 2011, barring the occurrence of certain specified events, which generally involve a material and imminent breach of our supply obligations at any specified facility.

We utilize local currency credit facilities to finance the operations of certain foreign subsidiaries. At June 30, 2011, \$29.5 million was outstanding under these facilities with no additional availability.

The weighted-average interest rate of our long-term debt outstanding at June 30, 2011 was 8.1% and 8.2% as of December 31, 2010.

5. FAIR VALUE

The fair value accounting guidance defines fair value as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date." The definition is based on an exit price rather than an entry price, regardless of whether the entity plans to hold or sell the asset. This guidance also establishes a fair value hierarchy to prioritize inputs used in measuring fair value as follows:

- Level 1: Observable inputs such as quoted prices in active markets;
- Level 2: Inputs, other than quoted prices in active markets, that are observable either directly or indirectly; and
- Level 3: Unobservable inputs in which there is little or no market data, which require the reporting entity to develop its own assumptions.

AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Financial instruments The estimated fair value of our financial assets and liabilities that are recognized at fair value on a recurring basis, using available market information and other observable data, as of June 30, 2011, are as follows:

Balance Sheet Classification	June 30, 2011		December 31, 2010		Input
	Carrying Amount (in millions)	Fair Value	Carrying Amount (in millions)	Fair Value	
Cash equivalents	\$105.6	\$105.6	\$152.5	\$152.5	Level 1
Prepaid expenses and other current assets					
Currency forward contracts	2.2	2.2	1.3	1.3	Level 2
Other assets and deferred charges					
Currency forward contracts	0.2	0.2	—	—	Level 2

The carrying value of our cash, accounts receivable, accounts payable and accrued liabilities approximates their fair values due to the short-term maturities of these instruments. The carrying value of our borrowings under the foreign credit facilities approximates their fair value due to the frequent resetting of the interest rates. We estimated the fair value of the amounts outstanding on our debt using available market information and other observable data, to be as follows:

	June 30, 2011		December 31, 2010		Input
	Carrying Amount (in millions)	Fair Value	Carrying Amount (in millions)	Fair Value	
9.25% Notes	\$378.7	\$416.9	\$420.3	\$473.9	Level 2
7.875% Notes	300.0	300.0	300.0	306.0	Level 2
5.25% Notes	249.9	247.2	249.9	245.0	Level 2

6. DERIVATIVES

Our business and financial results are affected by fluctuations in world financial markets, including interest rates and currency exchange rates. Our hedging policy has been developed to manage these risks to an acceptable level based on management's judgment of the appropriate trade-off between risk, opportunity and cost. We do not hold financial instruments for trading or speculative purposes.

Currency forward contracts From time to time, we use foreign currency forward contracts to reduce the effects of fluctuations in exchange rates, primarily relating to the Mexican Peso. As of June 30, 2011, we have forward contracts outstanding with a notional amount of \$57.9 million that hedge our exposure to changes in foreign currency exchange rates for our payroll expenses.

The following table summarizes the reclassification of pre-tax derivative gains into net income from accumulated other comprehensive income (loss):

Location of	Gain Reclassified	Gain Expected to be
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	Gain Reclassified into Net Income	Three Months Ended June 30, 2011 2010 (in millions)		Six Months Ended June 30, 2011 2010		Reclassified During the Next 12 Months
Currency forward contracts	Cost of Goods Sold	\$1.5	\$—	\$2.2	\$—	\$2.2

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AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

7. EMPLOYEE BENEFIT PLANS

The components of net periodic benefit cost are as follows:

	Pension Benefits			
	Three Months Ended June 30, 2011		Six Months Ended June 30, 2011	
	2010	2010	2010	2010
	(in millions)			
Service cost	\$1.1	\$1.3	\$2.2	\$2.5
Interest cost	9.2	9.2	18.4	18.5
Expected asset return	(7.9	) (8.0	) (15.8	) (16.0
Amortized loss	1.1	0.6	2.2	1.2
Net periodic benefit cost	\$3.5	\$3.1	\$7.0	\$6.2
	Other Postretirement Benefits			
	Three Months Ended June 30, 2011		Six Months Ended June 30, 2011	
	2010	2010	2010	2010
	(in millions)			
Service cost	\$0.2	\$0.2	\$0.4	\$0.5
Interest cost	4.3	4.0	8.6	8.0
Amortized gain	0.1	(0.4	) 0.2	(0.7
Amortized prior service credit	(0.8	) (0.7	) (1.6	) (1.5
Net periodic benefit cost	\$3.8	\$3.1	\$7.6	\$6.3

Our regulatory pension funding requirements in 2011 are approximately \$25 million. We expect our cash outlay for other postretirement benefit obligations in 2011, net of GM cost sharing, to be approximately \$15 million.

AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

8. PRODUCT WARRANTIES

We record a liability for estimated warranty obligations at the dates our product are sold. These estimates are established using sales volumes and internal and external warranty data where there is no payment history and historical information about the average cost of warranty claims for customers with prior claims. We adjust the liability as necessary.

As part of the 2009 Settlement and Commercial Agreement, AAM agreed to expanded warranty cost sharing with GM starting on January 1, 2011.

The following table provides a reconciliation of changes in the product warranty liability:

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2011	2010	2011	2010
	(in millions)			
Beginning balance	\$5.3	\$2.0	\$2.3	\$2.1
Accruals	3.1	0.2	6.1	0.4
Settlements	(0.3	) (0.1	) (0.4	) (0.2
Adjustment to prior period accruals	(0.1	) (0.1	) —	) (0.2
Foreign currency translation and other	0.1	—	0.1	(0.1
Ending balance	\$8.1	\$2.0	\$8.1	\$2.0

9. INCOME TAXES

We are required to adjust our effective tax rate each quarter to consistently estimate our annual effective tax rate. We must also record the tax impact of certain discrete items, unusual or infrequently occurring, including changes in judgment about valuation allowances and effects of changes in tax laws or rates, in the interim period in which they occur. In addition, jurisdictions with a projected loss for the year or a year-to-date loss where no tax benefit can be recognized are excluded from the estimated annual effective tax rate. The impact of such an exclusion could result in a higher or lower effective tax rate during a particular quarter, based upon the mix and timing of actual earnings versus annual projections.

Income tax expense (benefit) was a benefit of \$0.2 million in the three months ended June 30, 2011 and expense of \$1.9 million in the first six months of 2011 as compared to expense of \$2.4 million in the three months ended June 30, 2010 and expense of \$4.4 million in the first six months of 2010. Our effective income tax rate was negative 0.5% in the second quarter of 2011 and 2.2% in the first six months of 2011 as compared to 8.4% in the second quarter of 2010 and 9.5% in the first six months of 2010. Our income tax expense (benefit) and effective tax rate for the three and six months ended June 30, 2011 reflects the effect of recognizing a net operating loss benefit against our taxable income in the U.S. Our income tax expense (benefit) for the three and six months ended June 30, 2011 also reflects net tax benefits of \$2.8 million relating to the favorable resolution of income tax audits and the reversal of state deferred tax liabilities due to newly enacted Michigan tax legislation. Our income tax expense and effective tax rate for the three and six months ended June 30, 2010 reflected the effect of recording a valuation allowance against income tax benefits on U.S. losses.

In the second quarter of 2011, we settled our 2004 through 2007 U.S. federal income tax audits. As a result of the settlement, in addition to a favorable tax benefit adjustment of \$1.3 million included above, our gross unrecognized tax benefits were reduced by \$28.7 million, our deferred tax assets were reduced by \$22.3 million and our income tax payable increased by \$5.1 million.

AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

10. COMPREHENSIVE INCOME

Comprehensive income consists of the following:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
	(in millions)			
Net income	\$47.9	\$25.3	\$84.5	\$41.5
Defined benefit plans, net of tax	0.4	(0.3	) 3.5	2.0
Foreign currency translation adjustments, net of tax	8.3	(2.8	) 13.5	(8.0
Change in derivatives, net of tax	(0.1	) 0.1	1.1	0.1
Comprehensive income	\$56.5	\$22.3	\$102.6	\$35.6
Net loss attributable to noncontrolling interests	1.3	0.1	2.4	0.2
Foreign currency translation adjustments related to noncontrolling interests	—	(0.1	) (0.8) —
Comprehensive income attributable to AAM	\$57.8	\$22.3	\$104.2	\$35.8

11. EARNINGS PER SHARE (EPS)

The following table sets forth the computation of our basic and diluted EPS:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
	(in millions, except per share data)			
Numerator				
Net income attributable to AAM	\$49.2	\$25.4	\$86.9	\$41.7
Denominator				
Basic shares outstanding -				
Weighted-average shares outstanding	75.4	71.5	74.5	71.5
Effect of dilutive securities				
Dilutive stock-based compensation	—	0.1	0.2	0.1
Dilutive GM warrants	—	2.9	0.7	2.9
Diluted shares outstanding -				
Adjusted weighted-average shares after assumed conversions	75.4	74.5	75.4	74.5
Basic EPS	\$0.65	\$0.36	\$1.17	\$0.58
Diluted EPS	\$0.65	\$0.34	\$1.15	\$0.56

Certain exercisable stock options were excluded in the computations of diluted EPS because the exercise price of these options was greater than the average period market prices. The number of stock options outstanding, which were

not included in the calculation of diluted EPS, was 4.1 million at June 30, 2011 and 4.8 million at June 30, 2010. The ranges of exercise prices related to the excluded exercisable stock options were \$15.56 - \$40.83 at June 30, 2011 and \$10.08 - \$40.83 at June 30, 2010.

AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

As part of the 2009 Settlement and Commercial Agreement, we issued to GM five year warrants, which entitled GM to purchase 4.1 million shares of AAM's common stock at an exercise price of \$2.76 per share. In the first quarter of 2011, GM exercised these warrants. In accordance with the cashless exercise option available in the agreement, we issued 3.3 million net shares of common stock to GM.

12. SUPPLEMENTAL GUARANTOR CONDENSED CONSOLIDATING FINANCIAL STATEMENTS

Holdings has no significant assets other than its 100% ownership in AAM, Inc. and no direct subsidiaries other than AAM, Inc. Holdings fully and unconditionally guarantees the 5.25% Notes and 7.875% Notes, which are senior unsecured obligations of AAM, Inc. The 2.00% Convertible Notes are senior unsecured obligations of Holdings and are fully and unconditionally guaranteed by AAM, Inc.

The following Condensed Consolidating Financial Statements are included in lieu of providing separate financial statements for Holdings and AAM, Inc. These Condensed Consolidating Financial Statements are prepared under the equity method of accounting whereby the investments in subsidiaries are recorded at cost and adjusted for the parent's share of the subsidiaries' cumulative results of operations, capital contributions and distributions, and other equity changes.

AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Condensed Consolidating Statements of Operations

Three Months Ended June 30,

(in millions)

	Holdings	AAM Inc.	All Others	Elims	Consolidated
2011					
Net sales					
External	\$—	\$219.3	\$466.9	\$—	\$686.2
Intercompany	—	6.4	54.3	(60.7)) —
Total net sales	—	225.7	521.2	(60.7)	) 686.2
Cost of goods sold	—	203.8	412.6	(60.7)	) 555.7
Gross profit	—	21.9	108.6	—	130.5
Selling, general and administrative expenses	—	48.3	10.5	—	58.8
Operating income (loss)	—	(26.4)	) 98.1	—	71.7
Non-operating income (expense), net	—	(25.0)	) 1.0	—	(24.0)
Income (loss) before income taxes	—	(51.4)	) 99.1	—	47.7
Income tax expense (benefit)	—	(2.3)	) 2.1	—	(0.2)
Earnings from equity in subsidiaries	49.2	47.9	—	(97.1)) —
Net income (loss) before royalties and dividends	49.2	(1.2)	) 97.0	(97.1)	) 47.9
Royalties and dividends	—	50.4	(50.4)) —	—
Net income after royalties and dividends	49.2	49.2	46.6	(97.1)	) 47.9
Net loss attributable to noncontrolling interests	—	—	1.3	—	1.3
Net income attributable to AAM	\$49.2	\$49.2	\$47.9	\$(97.1)	) \$49.2
2010					
Net sales					
External	\$—	\$136.7	\$422.9	\$—	\$559.6
Intercompany	—	7.4	45.1	(52.5)) —
Total net sales	—	144.1	468.0	(52.5)	) 559.6
Cost of goods sold	—	134.0	379.2	(52.5)	) 460.7
Gross profit	—	10.1	88.8	—	98.9
Selling, general and administrative expenses	—	44.5	4.0	—	48.5
Operating income (loss)	—	(34.4)	) 84.8	—	50.4
Non-operating expense, net	—	(22.0)	) (0.7)	) —	(22.7)
Income (loss) before income taxes	—	(56.4)	) 84.1	—	27.7
Income tax expense	—	0.5	1.9	—	2.4
Earnings from equity in subsidiaries	25.4	62.5	—	(87.9)) —
Net income before royalties and dividends	25.4	5.6	82.2	(87.9)	) 25.3
Royalties and dividends	—	19.8	(19.8)) —	—
Net income after royalties and dividends	25.4	25.4	62.4	(87.9)	) 25.3
Net loss attributable to noncontrolling interests	—	—	0.1	—	0.1
Net income attributable to AAM	\$25.4	\$25.4	\$62.5	\$(87.9)	) \$25.4

AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Condensed Consolidating Statements of Operations

Six Months Ended June 30,

(in millions)

	Holdings	AAM Inc.	All Others	Elims	Consolidated
2011					
Net sales					
External	\$—	\$414.9	\$916.9	\$—	\$1,331.8
Intercompany	—	12.3	102.0	(114.3)	—
Total net sales	—	427.2	1,018.9	(114.3)	1,331.8
Cost of goods sold	—	386.6	813.6	(114.3)	1,085.9
Gross profit	—	40.6	205.3	—	245.9
Selling, general and administrative expenses	—	96.0	19.5	—	115.5
Operating income (loss)	—	(55.4)	185.8	—	130.4
Non-operating income (expense), net	—	(47.0)	3.0	—	(44.0)
Income (loss) before income taxes	—	(102.4)	188.8	—	86.4
Income tax expense (benefit)	—	(2.0)	3.9	—	1.9
Earnings from equity in subsidiaries	86.9	87.9	—	(174.8)	—
Net income (loss) before royalties and dividends	86.9	(12.5)	184.9	(174.8)	84.5
Royalties and dividends	—	99.4	(99.4)	—	—
Net income after royalties and dividends	86.9	86.9	85.5	(174.8)	84.5
Net loss attributable to noncontrolling interests	—	—	2.4	—	2.4
Net income attributable to AAM	\$86.9	\$86.9	\$87.9	\$(174.8)	\$86.9
2010					
Net sales					
External	\$—	\$255.0	\$826.5	\$—	\$1,081.5
Intercompany	—	14.4	84.5	(98.9)	—
Total net sales	—	269.4	911.0	(98.9)	1,081.5
Cost of goods sold	—	262.7	731.5	(98.9)	895.3
Gross profit	—	6.7	179.5	—	186.2
Selling, general and administrative expenses	—	86.3	7.5	—	93.8
Operating income (loss)	—	(79.6)	172.0	—	92.4
Non-operating expense, net	—	(44.5)	(2.0)	—	(46.5)
Income (loss) before income taxes	—	(124.1)	170.0	—	45.9
Income tax expense	—	0.2	4.2	—	4.4
Earnings from equity in subsidiaries	41.7	127.5	—	(169.2)	—
Net income before royalties and dividends	41.7	3.2	165.8	(169.2)	41.5
Royalties and dividends	—	38.5	(38.5)	—	—
Net income after royalties and dividends	41.7	41.7	127.3	(169.2)	41.5
Net loss attributable to noncontrolling interests	—	—	0.2	—	0.2
Net income attributable to AAM	\$41.7	\$41.7	\$127.5	\$(169.2)	\$41.7

AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Condensed Consolidating Balance Sheets
(in millions)

	Holdings	AAM Inc.	All Others	Elims	Consolidated
June 30, 2011					
Assets					
Current assets					
Cash and cash equivalents	\$—	\$62.0	\$188.3	\$—	\$250.3
Accounts receivable, net	—	37.4	161.6	—	199.0
Inventories, net	—	41.8	106.7	—	148.5
Prepaid expense and other current assets	—	31.3	49.5	—	80.8
Total current assets	—	172.5	506.1	—	678.6
Property, plant and equipment, net	—	248.5	711.9	—	960.4
Goodwill	—	—	156.6	—	156.6
Other assets and deferred charges	—	302.5	97.3	—	399.8
Investment in subsidiaries	—	991.2	—	(991.2)	—
Total assets	\$—	\$1,714.7	\$1,471.9	\$(991.2)	\$2,195.4
Liabilities and stockholders' equity (deficit)					
Current liabilities					
Accounts payable	\$—	\$106.8	\$248.2	\$—	\$355.0
Accrued expenses and other current liabilities	—	194.7	78.8	—	273.5
Total current liabilities	—	301.5	327.0	—	628.5
Intercompany payable (receivable)	320.7	(351.1)	30.4	—	—
Long-term debt	—	928.6	36.0	—	964.6
Investment in subsidiaries obligation	47.0	—	—	(47.0)	—
Other long-term liabilities	—	882.7	77.5	—	960.2
Total liabilities	367.7	1,761.7	470.9	(47.0)	2,553.3
Total AAM stockholders' equity (deficit)	(367.7)	(47.0)	991.2	(944.2)	(367.7)
Noncontrolling interest in subsidiaries	—	—	9.8	—	9.8
Total stockholders' equity (deficit)	(367.7)	(47.0)	1,001.0	(944.2)	(357.9)
Total liabilities and stockholders' equity (deficit)	\$—	\$1,714.7	\$1,471.9	\$(991.2)	\$2,195.4
December 31, 2010					
Assets					
Current assets					
Cash and cash equivalents	\$—	\$67.6	\$177.0	\$—	\$244.6
Accounts receivable, net	—	18.4	128.2	—	146.6
Inventories, net	—	34.8	95.5	—	130.3
Other current assets	—	35.6	45.0	—	80.6
Total current assets	—	156.4	445.7	—	602.1
Property, plant and equipment, net	—	259.6	676.7	—	936.3
Goodwill	—	—	155.8	—	155.8
Other assets and deferred charges	—	329.8	90.7	—	420.5
Investment in subsidiaries	—	887.7	—	(887.7)	—
Total assets	\$—	\$1,633.5	\$1,368.9	\$(887.7)	\$2,114.7
Liabilities and stockholders' equity (deficit)					
Current liabilities					
Accounts payable	\$—	\$76.4	\$207.2	\$—	\$283.6

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Accrued expenses and other current liabilities	—	209.9	75.6	—	285.5	
Total current liabilities	—	286.3	282.8	—	569.1	
Intercompany payable (receivable)	320.1	(395.3	) 75.2	—	—
Long-term debt	0.4	970.2	39.4	—	1,010.0	
Investment in subsidiaries obligation	159.0	—	—	(159.0) —	
Other long-term liabilities	—	931.3	72.4	—	1,003.7	
Total liabilities	479.5	1,792.5	469.8	(159.0	) 2,582.8
Total AAM stockholders' equity (deficit)	(479.5) (159.0) 887.7	(728.7) (479.5)
Noncontrolling interest in subsidiaries	—	—	11.4	—	11.4	
Total stockholders' equity (deficit)	(479.5) (159.0) 899.1	(728.7) (468.1)
Total liabilities and stockholders' equity (deficit)	\$—	\$1,633.5	\$1,368.9	\$(887.7) \$2,114.7	

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AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Condensed Consolidating Statements of Cash Flows

Six Months Ended June 30,

(in millions)

	Holdings	AAM Inc.	All Others	Elims	Consolidated
2011					
Operating activities					
Net cash provided by operating activities	\$—	\$0.2	\$116.3	\$—	\$116.5
Investing activities					
Purchases of property, plant and equipment	—	(16.5	) (55.1	) —	(71.6
Proceeds from sale of equipment	—	1.4	6.4	—	7.8
Net cash used in investing activities	—	(15.1	) (48.7	) —	(63.8
Financing activities					
Net debt activity	(42.9	) —	(4.5	) —	(47.4
Intercompany activity	43.0	10.0	(53.0) —	—
Debt issuance costs	—	(5.3	) —	—	(5.3
Employee stock option exercises	—	4.6	—	—	4.6
Purchase of treasury stock	(0.1	) —	—	—	(0.1
Net cash provided by (used in) financing activities	—	9.3	(57.5	) —	(48.2
Effect of exchange rate changes on cash	—	—	1.2	—	1.2
Net increase (decrease) in cash and cash equivalents	—	(5.6	) 11.3	—	5.7
Cash and cash equivalents at beginning of period	—	67.6	177.0	—	244.6
Cash and cash equivalents at end of period	\$—	\$62.0	\$188.3	\$—	\$250.3
2010					
Operating activities					
Net cash provided by (used in) operating activities	\$—	\$(32.4	) \$197.3	\$—	\$164.9
Investing activities					
Purchases of property, plant and equipment	—	(12.5	) (24.4	) —	(36.9
Proceeds from sale of equipment	—	1.1	0.1	—	1.2
Purchase buyouts of leased equipment	—	(7.4	) —	—	(7.4
Redemption of short-term investments	—	1.6	—	—	1.6
Net cash used in investing activities	—	(17.2	) (24.3	) —	(41.5
Financing activities					
Net debt activity	—	(59.6	) 2.1	—	(57.5
Intercompany activity	1.3	86.9	(88.2) —	—
Debt issuance costs	—	(2.2	) —	—	(2.2
Purchase of treasury stock	(1.3	) —	—	—	(1.3
Net cash provided by (used in) financing activities	—	25.1	(86.1	) —	(61.0
Effect of exchange rate changes on cash	—	—	(1.8	) —	(1.8
Net increase (decrease) in cash and cash equivalents	—	(24.5	) 85.1	—	60.6
	—	80.6	97.5	—	178.1

Cash and cash equivalents at beginning of
period

Cash and cash equivalents at end of period	\$—	\$56.1	\$182.6	\$—	\$238.7
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AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

13. SUPPLEMENTAL GUARANTOR CONDENSED CONSOLIDATING FINANCIAL STATEMENTS – 9.25% NOTES

Holdings has no significant asset other than its 100% ownership in AAM, Inc. and no direct subsidiaries other than AAM, Inc. The 9.25% Notes are senior secured obligations of AAM Inc. and are fully and unconditionally guaranteed by Holdings and all domestic subsidiaries of AAM, Inc.

These Condensed Consolidating Financial Statements are prepared under the equity method of accounting whereby the investments in subsidiaries are recorded at cost and adjusted for the parent's share of the subsidiaries' cumulative results of operations, capital contributions and distributions, and other equity changes.

Condensed Consolidating Statements of Operations

Three Months Ended June 30,

(in millions)

	Holdings	AAM Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Elims	Consolidated
2011						
Net sales						
External	\$—	\$219.3	\$49.2	\$ 417.7	\$—	\$686.2
Intercompany	—	6.4	52.0	2.3	(60.7)	—
Total net sales	—	225.7	101.2	420.0	(60.7)	686.2
Cost of goods sold	—	203.8	86.3	326.3	(60.7)	555.7
Gross profit	—	21.9	14.9	93.7	—	130.5
Selling, general and administrative expenses	—	48.3	—	10.5	—	58.8
Operating income (loss)	—	(26.4)	14.9	83.2	—	71.7
Non-operating income (expense), net	—	(25.0)	0.2	0.8	—	(24.0)
Income (loss) before income taxes	—	(51.4)	15.1	84.0	—	47.7
Income tax expense (benefit)	—	(2.3)	—	2.1	—	(0.2)
Earnings (loss) from equity in subsidiaries	49.2	47.9	(6.2)	—	(90.9)	—
Net income (loss) before royalties and dividends	49.2	(1.2)	8.9	81.9	(90.9)	47.9
Royalties and dividends	—	50.4	—	(50.4)	—	—
Net income after royalties and dividends	49.2	49.2	8.9	31.5	(90.9)	47.9
Net loss attributable to noncontrolling interests	—	—	—	1.3	—	1.3
Net income attributable to AAM	\$49.2	\$49.2	\$8.9	\$ 32.8	\$(90.9)	\$49.2

AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

	Holdings	AAM Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Elims	Consolidated
2010						
Net sales						
External	\$—	\$136.7	\$46.1	\$376.8	\$—	\$559.6
Intercompany	—	7.4	40.2	4.9	(52.5)	—
Total net sales	—	144.1	86.3	381.7	(52.5)	559.6
Cost of goods sold	—	134.0	86.3	292.9	(52.5)	460.7
Gross profit	—	10.1	—	88.8	—	98.9
Selling, general and administrative expenses	—	44.5	—	4.0	—	48.5
Operating income (loss)	—	(34.4)	—	84.8	—	50.4
Non-operating income (expense), net	—	(22.0)	0.1	(0.8)	—	(22.7)
Income (loss) before income taxes	—	(56.4)	0.1	84.0	—	27.7
Income tax expense	—	0.5	—	1.9	—	2.4
Earnings (loss) from equity in subsidiaries	25.4	62.5	(8.6)	—	(79.3)	—
Net income (loss) before royalties and dividends	25.4	5.6	(8.5)	82.1	(79.3)	25.3
Royalties and dividends	—	19.8	—	(19.8)	—	—
Net income (loss) after royalties and dividends	25.4	25.4	(8.5)	62.3	(79.3)	25.3
Net loss attributable to noncontrolling interests	—	—	—	0.1	—	0.1
Net income (loss) attributable to AAM	\$25.4	\$25.4	\$(8.5)	\$62.4	\$(79.3)	\$25.4

AMERICAN AXLE & MANUFACTURING HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Condensed Consolidating Statements of Operations

Six Months Ended June 30,

(in millions)

	Holdings	AAM Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Elims	Consolidated
2011						
Net sales						
External	\$—	\$414.9	\$100.2	\$ 816.7	\$—	\$1,331.8
Intercompany	—	12.3	97.0	5.0	(114.3)	—
Total net sales	—	427.2	197.2	821.7	(114.3)	1,331.8
Cost of goods sold	—	386.6	169.6	644.0	(114.3)	1,085.9
Gross profit	—	40.6	27.6	177.7	—	245.9
Selling, general and administrative expenses	—	96.0	—	19.5	—	115.5
Operating income (loss)	—	(55.4)	27.6	158.2	—	130.4
Non-operating income (expense), net	—	(47.0)	0.6	2.4	—	(44.0)
Income (loss) before income taxes	—	(102.4)	28.2	160.6	—	86.4
Income tax expense (benefit)	—	(2.0)	—	3.9	—	1.9
Earnings (loss) from equity in subsidiaries	86.9	87.9	(17.5)	—	(157.3)	—
Net income (loss) before royalties and dividends	86.9	(12.5				