OWENS ILLINOIS INC /DE/
Form 10-Q
April 26, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

FORM 10-Q

(Mark one)

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

For the quarterly period ended

March 31, 2012

or

o **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 1-9576

OWENS-ILLINOIS, INC.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**22-2781933** (IRS Employer Identification No.)
One Michael Owens Way, Perrysburg, Ohio (Address of principal executive offices)	**43551** (Zip Code)

Registrant s telephone number, including area code: **(567) 336-5000**

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 x No o

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 x No o

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 the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer x	Accelerated filer o
Non-accelerated filer o (do not check if a smaller reporting company)	Smaller reporting company o

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

The number of shares of common stock, par value $.01, of Owens-Illinois, Inc. outstanding as of March 31, 2012 was 164,926,375.

Part I FINANCIAL INFORMATION

Item 1. Financial Statements.

The Condensed Consolidated Financial Statements of Owens-Illinois, Inc. (the Company) presented herein are unaudited but, in the opinion of management, reflect all adjustments necessary to present fairly such information for the periods and at the dates indicated. All adjustments are of a normal recurring nature. Because the following unaudited condensed consolidated financial statements have been prepared in accordance with Article 10 of Regulation S-X, they do not contain all information and footnotes normally contained in annual consolidated financial statements; accordingly, they should be read in conjunction with the Consolidated Financial Statements and notes thereto appearing in the Company s Annual Report on Form 10-K for the year ended December 31, 2011.

OWENS-ILLINOIS, INC.

CONDENSED CONSOLIDATED RESULTS OF OPERATIONS

(Dollars in millions, except per share amounts)

	Three months ended March 31, 2012	2011
Net sales	$ 1,739	$ 1,719
Manufacturing, shipping and delivery expense	(1,361)	(1,376)
Gross profit	378	343
Selling and administrative expense	(140)	(142)
Research, development and engineering expense	(15)	(16)
Interest expense	(64)	(76)
Interest income	3	3
Equity earnings	13	14
Royalties and net technical assistance	4	5
Other income	2	2
Other expense	(11)	(18)
Earnings from continuing operations before income taxes	170	115
Provision for income taxes	(44)	(28)
Earnings from continuing operations	126	87
Loss from discontinued operations	(1)	(1)
Net earnings	125	86
Net earnings attributable to noncontrolling interests	(4)	(4)
Net earnings attributable to the Company	$ 121	$ 82
Amounts attributable to the Company:		
Earnings from continuing operations	$ 122	$ 83
Loss from discontinued operations	(1)	(1)
Net earnings	$ 121	$ 82
Basic earnings per share:		
Earnings from continuing operations	$ 0.74	$ 0.50
Loss from discontinued operations	(0.01)	
Net earnings	$ 0.73	$ 0.50
Weighted average shares outstanding (thousands)	164,241	163,355
Diluted earnings per share:		
Earnings from continuing operations	$ 0.73	$ 0.50
Loss from discontinued operations	(0.01)	
Net earnings	$ 0.72	$ 0.50
Weighted average diluted shares outstanding (thousands)	166,206	166,114

See accompanying notes.

OWENS-ILLINOIS, INC.

CONDENSED CONSOLIDATED COMPREHENSIVE INCOME

(Dollars in millions)

	Three months ended March 31, 2012	2011
Net earnings	$ 125	$ 86
Other comprehensive income, net of tax:		
Foreign currency translation adjustments	99	74
Pension and other postretirement benefit adjustments	24	20
Change in fair value of derivative instruments		1
Other comprehensive income	123	95
Total comprehensive income	248	181
Comprehensive income attributable to noncontrolling interests	(11)	(8)
Comprehensive income attributable to the Company	$ 237	$ 173

See accompanying notes.

OWENS-ILLINOIS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(Dollars in millions, except per share amounts)

	March 31, 2012	December 31, 2011	March 31, 2011
Assets			
Current assets:			
Cash and cash equivalents	$ 299	$ 400	$ 430
Receivables, less allowances for losses and discounts ($42 at March 31, 2012, $38 at December 31, 2011, and $43 at March 31, 2011)	1,199	1,158	1,223
Inventories	1,237	1,061	1,103
Prepaid expenses	130	124	78
Total current assets	2,865	2,743	2,834
Investments and other assets:			
Equity investments	316	315	301
Repair parts inventories	153	155	154
Pension assets	121	116	59
Other assets	695	687	634
Goodwill	2,127	2,082	2,900
Total other assets	3,412	3,355	4,048
Property, plant and equipment, at cost	7,049	6,899	7,213
Less accumulated depreciation	4,165	4,022	4,070
Net property, plant and equipment	2,884	2,877	3,143
Total assets	$ 9,161	$ 8,975	$ 10,025

CONDENSED CONSOLIDATED BALANCE SHEETS Continued

		March 31, 2012		December 31, 2011		March 31, 2011
Liabilities and Share Owners Equity						
Current liabilities:						
Short-term loans and long-term debt due within one year	$	406	$	406	$	372
Current portion of asbestos-related liabilities		165		165		170
Accounts payable		943		1,038		889
Other liabilities		602		636		646
Total current liabilities		2,116		2,245		2,077
Long-term debt		3,724		3,627		3,991
Deferred taxes		214		212		215
Pension benefits		856		871		576
Nonpension postretirement benefits		270		269		260
Other liabilities		410		404		403
Asbestos-related liabilities		276		306		273
Commitments and contingencies						
Share owners equity:						
Share owners equity of the Company:						
Common stock, par value $.01 per share, 250,000,000 shares authorized, 181,658,637, 181,174,050, and 181,051,389 shares issued (including treasury shares), respectively		2		2		2
Capital in excess of par value		2,996		2,991		3,041
Treasury stock, at cost, 16,732,262, 16,799,903, and 17,045,437 shares, respectively		(404)		(405)		(411)
Retained earnings (loss)		(258)		(379)		203
Accumulated other comprehensive loss		(1,205)		(1,321)		(806)
Total share owners equity of the Company		1,131		888		2,029
Noncontrolling interests		164		153		201
Total share owners equity		1,295		1,041		2,230
Total liabilities and share owners equity	$	9,161	$	8,975	$	10,025

See accompanying notes.

OWENS-ILLINOIS, INC.

CONDENSED CONSOLIDATED CASH FLOWS

(Dollars in millions)

	Three months ended March 31, 2012	2011
Cash flows from operating activities:		
Net earnings	$ 125	$ 86
Loss from discontinued operations	1	1
Non-cash charges (credits):		
Depreciation	97	101
Amortization of intangibles and other deferred items	8	5
Amortization of finance fees and debt discount	8	8
Pension expense	22	23
Restructuring and asset impairment		8
Other	10	11
Pension contributions	(17)	(12)
Asbestos-related payments	(30)	(33)
Cash paid for restructuring activities	(30)	(4)
Change in non-current assets and liabilities	(13)	(30)
Change in components of working capital	(275)	(249)
Cash utilized in continuing operating activities	(94)	(85)
Cash utilized in discontinued operating activities	(1)	
Total cash utilized in operating activities	(95)	(85)
Cash flows from investing activities:		
Additions to property, plant and equipment	(73)	(73)
Acquisitions, net of cash acquired	(5)	6
Net cash proceeds related to sale of assets and other	11	
Cash utilized in investing activities	(67)	(67)
Cash flows from financing activities:		
Additions to long-term debt	119	5
Repayments of long-term debt	(62)	(10)
Decrease in short-term loans	(20)	(32)
Net receipts (payments) for hedging activity	8	(12)
Dividends paid to noncontrolling interests		(18)
Issuance of common stock and other		2
Cash provided by (utilized in) financing activities	45	(65)
Effect of exchange rate fluctuations on cash	16	7
Decrease in cash	(101)	(210)
Cash at beginning of period	400	640
Cash at end of period	$ 299	$ 430

See accompanying notes.

OWENS-ILLINOIS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Tabular data dollars in millions, except per share amounts

1. Change in Accounting Method

Effective January 1, 2012, the Company elected to change the method of valuing U.S. inventories to the average cost method, while in prior years these inventories were valued using the last-in, first-out (LIFO) method. The Company believes the average cost method is preferable as it conforms the inventory costing methods globally, improves comparability with industry peers and better reflects the current value of inventory on the consolidated balance sheets. All prior periods presented have been adjusted to apply the new method retrospectively.

The effect of the change on the condensed consolidated results of operations for the quarter ended March 31, 2011 is as follows:

	As originally reported under LIFO	Effect of Change	As Adjusted
Manufacturing, shipping and delivery expense	$ (1,386)	$ 10	$ (1,376)
Amounts attributable to the Company:			
Net earnings from continuing operations	73	10	83
Basic earnings per share	0.44	0.06	0.50
Diluted earnings per share	0.44	0.06	0.50

The effect of the change on the condensed consolidated balance sheets as of December 31, 2011 and March 31, 2011 is as follows:

December 31, 2011	As originally reported under LIFO	Effect of Change	As Adjusted
Assets:			
Inventories	$ 1,012	$ 49	$ 1,061
Share owners equity:			
Retained earnings (loss)	(428)	49	(379)
March 31, 2011			
Assets:			
Inventories	$ 1,054	$ 49	$ 1,103
Share owners equity:			
Retained earnings	154	49	203

The effect of the change on the consolidated share owners equity as of January 1, 2011 is as follows:

	As originally reported under LIFO	Effect of Change	As Adjusted
Retained earnings	$ 82	$ 39	$ 121

The effect of the change on the condensed consolidated cash flows for the quarter ended March 31, 2011 is as follows:

	As originally reported under LIFO	Effect of Change	As Adjusted
Net earnings	$ 76	$ 10	$ 86
Change in components of working capital	(239)	(10)	(249)

Had the Company not made this change in accounting method, manufacturing, shipping and delivery expense for the quarter ended March 31, 2012 would have been $6 million lower and net earnings attributable to the Company would have been $6 million higher than reported in the condensed consolidated results of operations. In addition, both basic and diluted earnings per share would have been $0.04 higher.

2. Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share:

	Three months ended March 31, 2012		2011	
Numerator:				
Net earnings attributable to the Company	$	121	$	82
Denominator (in thousands):				
Denominator for basic earnings per share - weighted average shares outstanding		164,241		163,355
Effect of dilutive securities:				
Stock options and other		1,965		2,759
Denominator for diluted earnings per share - adjusted weighted average shares outstanding		166,206		166,114
Basic earnings per share:				
Earnings from continuing operations	$	0.74	$	0.50
Loss from discontinued operations		(0.01)		
Net earnings	$	0.73	$	0.50
Diluted earnings per share:				
Earnings from continuing operations	$	0.73	$	0.50
Loss from discontinued operations		(0.01)		
Net earnings	$	0.72	$	0.50

Options to purchase 956,580 and 462,037 weighted average shares of common stock which were outstanding during the three months ended March 31, 2012 and 2011, respectively, were not included in the computation of diluted earnings per share because the options exercise price was greater than the average market price of the common shares.

The 2015 Exchangeable Notes have a dilutive effect only in those periods in which the Company s average stock price exceeds the exchange price of $47.47 per share. For the three months ended March 31, 2012 and 2011, the Company s average stock price did not exceed the exchange price. Therefore, the potentially issuable shares resulting from the settlement of the 2015 Exchangeable Notes were not included in the calculation of diluted earnings per share.

3. Debt

The following table summarizes the long-term debt of the Company:

	March 31, 2012	December 31, 2011	March 31, 2011
Secured Credit Agreement:			
Revolving Credit Facility:			
Revolving Loans	$ 55	$	$
Term Loans:			
Term Loan A (170 million AUD)	177	173	
Term Loan B	600	600	
Term Loan C (116 million CAD)	117	114	
Term Loan D (141 million)	188	182	
Fourth Amended and Restated Secured Credit Agreement:			
Term Loans:			
Term Loan A			93
Term Loan B			190
Term Loan C			114
Term Loan D			268
Senior Notes:			
6.75%, due 2014			400
6.75%, due 2014 (225 million)			318
3.00%, Exchangeable, due 2015	628	624	611
7.375%, due 2016	588	588	586
6.875%, due 2017 (300 million)	401	388	425
6.75%, due 2020 (500 million)	668	647	708
Senior Debentures:			
7.80%, due 2018	250	250	250
Other	139	137	163
Total long-term debt	3,811	3,703	4,126
Less amounts due within one year	87	76	135
Long-term debt	$ 3,724	$ 3,627	$ 3,991

On May 19, 2011, the Company s subsidiary borrowers entered into the Secured Credit Agreement (the Agreement). At March 31, 2012, the Agreement included a $900 million revolving credit facility, a 170 million Australian dollar term loan, a $600 million term loan, a 116 million Canadian dollar term loan, and a 141 million term loan, each of which has a final maturity date of May 19, 2016. At March 31, 2012, the Company s subsidiary borrowers had unused credit of $749 million available under the Agreement.

The weighted average interest rate on borrowings outstanding under the Agreement at March 31, 2012 was 2.82%.

The Company has a 280 million European accounts receivable securitization program, which extends through September 2016, subject to annual renewal of backup credit lines. Information related to the Company s accounts receivable securitization program is as follows:

	March 31, 2012	December 31, 2011	March 31, 2011
Balance (included in short-term loans)	$ 276	$ 281	$ 222
Weighted average interest rate	1.42%	2.41%	2.85%

The carrying amounts reported for the accounts receivable securitization programs, and certain long-term debt obligations subject to frequently redetermined interest rates, approximate fair value. Fair values for the Company s significant fixed rate debt obligations are based on published market quotations, and are classified as Level 1 in the fair value hierarchy.

Fair values at March 31, 2012 of the Company s significant fixed rate debt obligations are as follows:

	Principal Amount	Indicated Market Price	Fair Value
Senior Notes:			
3.00%, Exchangeable, due 2015	$ 690	98.12	$ 677
7.375%, due 2016	600	112.74	676
6.875%, due 2017 (300 million)	401	103.11	413
6.75%, due 2020 (500 million)	668	106.02	708
Senior Debentures:			
7.80%, due 2018	250	113.50	284

4. Supplemental Cash Flow Information

	Three months ended March 31, 2012	2011
Interest paid in cash	$ 69	$ 67
Income taxes paid in cash:		
Non-U.S.	31	21

5. Share Owners Equity

The activity in share owners equity for the three months ended March 31, 2012 and 2011 is as follows:

	Share Owners Equity of the Company						
	Common Stock	Capital in Excess of Par Value	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Loss	Non-controlling Interests	Total Share Owners Equity
Balance on January 1, 2012	$ 2	$ 2,991	$ (405)	$ (379)	$ (1,321)	$ 153	$ 1,041
Issuance of common stock (0.1 million shares)		1					1
Reissuance of common stock (0.07 million shares)			1				1
Stock compensation		4					4
Comprehensive income:							
Net earnings				121		4	125
Foreign currency translation adjustments					92	7	99
Pension and other postretirement benefit adjustments, net of tax					24		24
Balance on March 31, 2012	$ 2	$ 2,996	$ (404)	$ (258)	$ (1,205)	$ 164	$ 1,295

	Share Owners Equity of the Company						
	Common Stock	Capital in Excess of Par Value	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Loss	Non-controlling Interests	Total Share Owners Equity
Balance on January 1, 2011	$ 2	$ 3,040	$ (412)	$ 121	$ (897)	$ 211	$ 2,065
Issuance of common stock (0.2 million shares)		2					2
Reissuance of common stock (0.05 million shares)			1				1
Stock compensation		(1)					(1)
Comprehensive income:							
Net earnings				82		4	86
Foreign currency translation adjustments					70	4	74
Pension and other postretirement benefit adjustments, net of tax					20		20
Change in fair value of derivative instruments, net of tax					1		1
Dividends paid to noncontrolling interests on subsidiary common stock						(18)	(18)
Balance on March 31, 2011	$ 2	$ 3,041	$ (411)	$ 203	$ (806)	$ 201	$ 2,230

6. Inventories

Major classes of inventory are as follows:

	March 31, 2012	December 31, 2011	March 31, 2011
Finished goods	$ 1,061	$ 891	$ 932
Raw materials	126	123	114
Operating supplies	50	47	57
	$ 1,237	$ 1,061	$ 1,103

7. Contingencies

The Company is a defendant in numerous lawsuits alleging bodily injury and death as a result of exposure to asbestos dust. From 1948 to 1958, one of the Company s former business units commercially produced and sold approximately $40 million of a high-temperature, calcium-silicate based pipe and block insulation material containing asbestos. The Company exited the pipe and block insulation business in April 1958. The typical asbestos personal injury lawsuit alleges various theories of liability, including negligence, gross negligence and strict liability and seek compensatory and in some cases, punitive damages in various amounts (herein referred to as asbestos claims).

As of March 31, 2012, the Company has determined that it is a named defendant in asbestos lawsuits and claims involving approximately 4,700 plaintiffs and claimants. Based on an analysis of the lawsuits pending as of December 31, 2011, approximately 71% of plaintiffs either do not specify the monetary damages sought, or in the case of court filings, claim an amount sufficient to invoke the jurisdictional minimum of the trial court. Approximately 27% of plaintiffs specifically plead damages of $15 million or less, and 2% of plaintiffs specifically plead damages greater than $15 million but less than $100 million. Fewer than 1% of plaintiffs specifically plead damages $100 million or greater but less than $122 million.

As indicated by the foregoing summary, current pleading practice permits considerable variation in the assertion of monetary damages. The Company s experience resolving hundreds of thousands of asbestos claims and lawsuits over an extended period demonstrates that the monetary relief that may be alleged in a complaint bears little relevance to a claim s merits or disposition value. Rather, the amount potentially recoverable is determined by such factors as the severity of the plaintiff s asbestos disease, the product identification evidence against the Company and other defendants, the defenses available to the Company and other defendants, the specific jurisdiction in which the claim is made, and the plaintiff s medical history and exposure to other disease-causing agents.

In addition to the pending claims set forth above, the Company has claims-handling agreements in place with many plaintiffs counsel throughout the country. These agreements require evaluation and negotiation regarding whether particular claimants qualify under the criteria established by such agreements. The criteria for such claims include verification of a compensable illness and a reasonable probability of exposure to a product manufactured by the Company s former business unit during its manufacturing period ending in 1958. Some plaintiffs counsel have historically withheld claims under these agreements for later presentation while focusing their attention on active litigation in the tort system. The Company believes that as of March 31, 2012 there are approximately 350 claims against other defendants

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which are likely to be asserted some time in the future against the Company. These claims are not included in the pending lawsuits and claims totals set forth above.

The Company is also a defendant in other asbestos-related lawsuits or claims involving maritime workers, medical monitoring claimants, co-defendants and property damage claimants. Based upon its past experience, the Company believes that these categories of lawsuits and claims will not involve any material liability and they are not included in the above description of pending matters or in the following description of disposed matters.

Since receiving its first asbestos claim, the Company as of March 31, 2012, has disposed of the asbestos claims of approximately 388,000 plaintiffs and claimants at an average indemnity payment per claim of approximately $8,200. Certain of these dispositions have included deferred amounts payable over a number of years. Deferred amounts payable totaled approximately $35 million at March 31, 2012 ($18 million at December 31, 2011) and are included in the foregoing average indemnity payment per claim. The Company s asbestos indemnity payments have varied on a per claim basis, and are expected to continue to vary considerably over time. As discussed above, a part of the Company s objective is to achieve, where possible, resolution of asbestos claims pursuant to claims-handling agreements. Failure of claimants to meet certain medical and product exposure criteria in the Company s administrative claims handling agreements has generally reduced the number of marginal or suspect claims that would otherwise have been received. In addition, certain courts and legislatures have reduced or eliminated the number of marginal or suspect claims that the Company otherwise would have received. These developments generally have had the effect of increasing the Company s per-claim average indemnity payment.

The Company believes that its ultimate asbestos-related liability (i.e., its indemnity payments or other claim disposition costs plus related legal fees) cannot reasonably be estimated. Beginning with the initial liability of $975 million established in 1993, the Company has accrued a total of approximately $4.0 billion through 2011, before insurance recoveries, for its asbestos-related liability. The Company s ability to reasonably estimate its liability has been significantly affected by, among other factors, the volatility of asbestos-related litigation in the United States, the significant number of co-defendants that have filed for bankruptcy, the magnitude and timing of co-defendant bankruptcy trust payments, the inherent uncertainty of future disease incidence and claiming patterns, the expanding list of non-traditional defendants that have been sued in this litigation, and the use of mass litigation screenings to generate large numbers of claims by parties who allege exposure to asbestos dust but have no present physical asbestos impairment.

The Company has continued to monitor trends that may affect its ultimate liability and has continued to analyze the developments and variables affecting or likely to affect the resolution of pending and future asbestos claims against the Company. The material components of the Company s accrued liability are based on amounts determined by the Company in connection with its annual comprehensive review and consist of the following estimates, to the extent it is probable that such liabilities have been incurred and can be reasonably estimated: (i) the liability for asbestos claims already asserted against the Company; (ii) the liability for preexisting but unasserted asbestos claims for prior periods arising under its administrative claims-handling agreements with various plaintiffs counsel; (iii) the liability for asbestos claims not yet asserted against the Company, but which the Company believes will be asserted in the next several years; and (iv) the legal defense costs likely to be incurred in connection with the foregoing types of claims.

The significant assumptions underlying the material components of the Company s accrual are:

a) the extent to which settlements are limited to claimants who were exposed to the Company s asbestos-containing insulation prior to its exit from that business in 1958;

b) the extent to which claims are resolved under the Company s administrative claims agreements or on terms comparable to those set forth in those agreements;

c) the extent of decrease or increase in the incidence of serious disease cases and claiming patterns for such cases;

d) the extent to which the Company is able to defend itself successfully at trial;

e) the extent to which courts and legislatures eliminate, reduce or permit the diversion of financial resources for unimpaired claimants;

f) the number and timing of additional co-defendant bankruptcies;

g) the extent to which bankruptcy trusts direct resources to resolve claims that are also presented to the Company and the timing of the payments made by the bankruptcy trusts; and

h) the extent to which co-defendants with substantial resources and assets continue to participate significantly in the resolution of future asbestos lawsuits and claims.

As noted above, the Company conducts a comprehensive review of its asbestos-related liabilities and costs annually in connection with finalizing and reporting its annual results of operations, unless significant changes in trends or new developments warrant an earlier review. If the results of an annual comprehensive review indicate that the existing amount of the accrued liability is insufficient to cover its estimated future asbestos-related costs, then the Company will record an appropriate charge to increase the accrued liability. The Company believes that a reasonable estimation of the probable amount of the liability for claims not yet asserted against the Company is not possible beyond a period of several years. Therefore, while the results of future annual comprehensive reviews cannot be determined, the Company expects the addition of one year to the estimation period will result in an annual charge.