

AIR PRODUCTS & CHEMICALS INC /DE/

Form 10-Q

July 27, 2011

Table of Contents

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

FORM 10-Q

(Mark One)

☒ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended 30 June 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 1-4534

AIR PRODUCTS AND CHEMICALS, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or Other Jurisdiction of Incorporation or Organization)

23-1274455
(I.R.S. Employer Identification No.)

7201 Hamilton Boulevard, Allentown, Pennsylvania
(Address of Principal Executive Offices)

18195-1501
(Zip Code)

610-481-4911

(Registrant's Telephone Number, Including Area Code)

Not Applicable

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

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

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 ☒

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at July 18, 2011
Common Stock, \$1 par value	213,132,964

Table of Contents

AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries

INDEX

	Page No.
PART I. FINANCIAL INFORMATION	
Item 1. Financial Statements	
<u>Consolidated Balance Sheets 30 June 2011 and 30 September 2010</u>	3
<u>Consolidated Income Statements Three and Nine Months Ended 30 June 2011 and 2010</u>	4
<u>Consolidated Comprehensive Income Statements Three and Nine Months Ended 30 June 2011 and 2010</u>	5
<u>Consolidated Statements of Cash Flows Nine Months Ended 30 June 2011 and 2010</u>	6
<u>Notes to Consolidated Financial Statements</u>	7
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	22
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	36
Item 4. <u>Controls and Procedures</u>	37
PART II. OTHER INFORMATION	
Item 6. <u>Exhibits</u>	37
<u>Signatures</u>	38
<u>Exhibit Index</u>	39

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries****CONSOLIDATED BALANCE SHEETS****(Unaudited)**

	30 June	30 September
(Millions of dollars, except for share data)	2011	2010
Assets		
Current Assets		
Cash and cash items	\$ 430.1	\$ 374.3
Trade receivables, less allowances for doubtful accounts	1,649.8	1,481.9
Inventories	639.6	571.6
Contracts in progress, less progress billings	145.3	163.6
Prepaid expenses	101.2	70.3
Other receivables and current assets	310.5	372.1
Total Current Assets	3,276.5	3,033.8
Investments in Net Assets of and Advances to Equity Affiliates	1,035.6	912.8
Plant and Equipment, at cost	17,536.0	16,309.7
Less: Accumulated depreciation	10,011.8	9,258.4
Plant and Equipment, net	7,524.2	7,051.3
Goodwill	969.1	914.6
Intangible Assets, net	295.0	285.7
Noncurrent Capital Lease Receivables	948.1	770.4
Other Noncurrent Assets	403.0	537.3
Total Assets	\$14,451.5	\$13,505.9
Liabilities and Equity		
Current Liabilities		
Payables and accrued liabilities	\$ 1,582.7	\$ 1,702.0
Accrued income taxes	77.7	73.6
Short-term borrowings	430.4	286.0
Current portion of long-term debt	13.0	182.5
Total Current Liabilities	2,103.8	2,244.1
Long-Term Debt	4,054.3	3,659.8
Other Noncurrent Liabilities	1,425.6	1,569.3
Deferred Income Taxes	470.8	335.1
Total Liabilities	8,054.5	7,808.3
Commitments and Contingencies See Note 10		
Air Products Shareholders' Equity		
Common stock (par value \$1 per share; 2011 and 2010 249,455,584 shares)	249.4	249.4
Capital in excess of par value	800.1	802.2
Retained earnings	8,397.4	7,852.2
Accumulated other comprehensive income (loss)	(865.4)	(1,159.4)
Treasury stock, at cost (2011 36,322,620 shares; 2010 35,652,719 shares)	(2,349.3)	(2,197.5)
Total Air Products Shareholders' Equity	6,232.2	5,546.9
Noncontrolling Interests	164.8	150.7
Total Equity	6,397.0	5,697.6
Total Liabilities and Equity	\$14,451.5	\$13,505.9

The accompanying notes are an integral part of these statements.

Table of Contents**AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries****CONSOLIDATED INCOME STATEMENTS****(Unaudited)**

	Three Months Ended		Nine Months Ended	
	30 June		30 June	
(Millions of dollars, except for share data)	2011	2010	2011	2010
Sales	\$ 2,577.8	\$ 2,252.3	\$ 7,470.8	\$ 6,674.8
Cost of sales	1,882.1	1,611.0	5,405.1	4,808.3
Selling and administrative	252.9	241.2	756.9	725.7
Research and development	29.3	29.3	86.4	82.8
Net loss on Airgas transaction		37.9	48.5	61.3
Customer bankruptcy		(1.8)		(1.8)
Pension settlement		6.3		6.3
Other income, net	3.3	8.0	23.0	29.8
Operating Income	416.8	336.4	1,196.9	1,022.0
Equity affiliates income	39.7	32.5	99.2	91.6
Interest expense	26.5	30.0	86.9	91.1
Income from Continuing Operations before Taxes	430.0	338.9	1,209.2	1,022.5
Income tax provision	103.9	77.6	295.7	246.0
Income from Continuing Operations	326.1	261.3	913.5	776.5
Income from Discontinued Operations, net of tax	8.9		8.9	
Net Income	335.0	261.3	922.4	776.5
Less: Net Income Attributable to Noncontrolling Interests	8.5	8.1	23.0	19.5
Net Income Attributable to Air Products	\$ 326.5	\$ 253.2	\$ 899.4	\$ 757.0
Net Income Attributable to Air Products				
Income from continuing operations	\$ 317.6	\$ 253.2	\$ 890.5	\$ 757.0
Income from discontinued operations	8.9		8.9	
Net Income Attributable to Air Products	\$ 326.5	\$ 253.2	\$ 899.4	\$ 757.0
Basic Earnings Per Common Share Attributable to Air Products				
Income from continuing operations	\$ 1.50	\$ 1.19	\$ 4.17	\$ 3.57
Income from discontinued operations	.04		.04	
Net Income Attributable to Air Products	\$ 1.54	\$ 1.19	\$ 4.21	\$ 3.57
Diluted Earnings Per Common Share Attributable to Air Products				
Income from continuing operations	\$ 1.46	\$ 1.17	\$ 4.08	\$ 3.49
Income from discontinued operations	.04		.04	
Net Income Attributable to Air Products	\$ 1.50	\$ 1.17	\$ 4.12	\$ 3.49
Weighted Average of Common Shares Outstanding (in millions)	212.5	212.3	213.5	212.0
Weighted Average of Common Shares Outstanding Assuming Dilution (in millions)	217.3	216.9	218.4	216.9
Dividends Declared Per Common Share Cash	\$.58	\$.49	\$ 1.65	\$ 1.43

The accompanying notes are an integral part of these statements.

Table of Contents**AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries****CONSOLIDATED COMPREHENSIVE INCOME STATEMENTS****(Unaudited)**

	Three Months Ended	
	30 June	
(Millions of dollars)	2011	2010
Net Income	\$ 335.0	\$ 261.3
Other Comprehensive Income (Loss), net of tax:		
Translation adjustments, net of tax (benefit) of \$(11.5) and \$79.1	103.0	(195.7)
Net gain (loss) on derivatives, net of tax (benefit) of \$3.9 and \$(9.7)	5.3	(16.0)
Unrealized holding loss on available-for-sale securities, net of tax benefit of \$(1.2)		(2.0)
Pension and postretirement benefits, net of tax of \$2.6		4.1
Reclassification adjustments:		
Currency translation adjustment		(.7)
Derivatives, net of tax (benefit) of \$(3.3) and \$9.4	(4.9)	15.7
Pension and postretirement benefits, net of tax of \$8.7 and \$8.7	16.8	16.1
Total Other Comprehensive Income (Loss)	120.2	(178.5)
Comprehensive Income	455.2	82.8
Comprehensive Income Attributable to Noncontrolling Interests	11.9	5.7
Comprehensive Income Attributable to Air Products	\$ 443.3	\$ 77.1

	Nine Months Ended	
	30 June	
(Millions of dollars)	2011	2010
Net Income	\$ 922.4	\$ 776.5
Other Comprehensive Income (Loss), net of tax:		
Translation adjustments, net of tax of \$31.6 and \$135.7	267.4	(126.5)
Net (loss) on derivatives, net of tax (benefit) of \$5.3 and \$(14.5)	7.7	(25.3)
Unrealized holding gain (loss) on available-for-sale securities, net of tax (benefit) of \$(3.3) and \$8.4	(4.6)	14.5
Pension and postretirement benefits, net of tax of \$2.6		4.1
Reclassification adjustments:		
Currency translation adjustment		(.7)
Derivatives, net of tax (benefit) of \$(0.3) and \$13.1	0.5	23.5
Available-for-sale securities, net of tax benefit of \$(9.3)	(16.1)	
Pension and postretirement benefits, net of tax of \$26.1 and \$21.3	50.4	39.8
Total Other Comprehensive Income (Loss)	305.3	(70.6)
Comprehensive Income	1,227.7	705.9
Comprehensive Income Attributable to Noncontrolling Interests	34.3	17.6
Comprehensive Income Attributable to Air Products	\$1,193.4	\$ 688.3

The accompanying notes are an integral part of these statements.

Table of Contents**AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries****CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited)**

	Nine Months Ended	
	30 June	
(Millions of dollars)	2011	2010
Operating Activities		
Net Income	\$ 922.4	\$ 776.5
Less: Net income attributable to noncontrolling interests	23.0	19.5
Net income attributable to Air Products	\$ 899.4	\$ 757.0
Adjustments to reconcile income to cash provided by operating activities:		
Depreciation and amortization	657.3	648.8
Deferred income taxes	74.2	80.7
Undistributed earnings of unconsolidated affiliates	(18.4)	(35.2)
Gain on sale of assets and investments	(6.1)	(9.1)
Share-based compensation	33.1	36.6
Noncurrent capital lease receivables	(155.7)	(72.7)
Net loss on Airgas transaction	48.5	61.3
Payment of acquisition-related costs	(156.2)	(8.8)
Other adjustments	59.4	39.3
Working capital changes that provided (used) cash, excluding effects of acquisitions and divestitures:		
Trade receivables	(105.5)	(151.3)
Inventories	(43.9)	(9.5)
Contracts in progress, less progress billings	20.9	4.6
Other receivables	3.0	(8.4)
Payables and accrued liabilities	(167.6)	(315.9)
Other working capital	(13.7)	15.8
Cash Provided by Operating Activities	1,128.7	1,033.2
Investing Activities		
Additions to plant and equipment	(965.3)	(757.2)
Acquisitions, less cash acquired	(9.9)	(37.2)
Investment in and advances to unconsolidated affiliates	(46.0)	(4.7)
Investment in Airgas stock		(69.6)
Proceeds from sale of Airgas stock	94.7	
Proceeds from sale of assets and investments	62.3	32.6
Change in restricted cash	13.0	28.2
Cash Used for Investing Activities	(851.2)	(807.9)
Financing Activities		
Long-term debt proceeds	59.2	110.9
Payments on long-term debt	(182.4)	(109.8)
Net increase (decrease) in commercial paper and short-term borrowings	411.9	(50.0)
Dividends paid to shareholders	(333.0)	(294.6)
Purchase of treasury stock	(350.0)	
Proceeds from stock option exercises	124.4	42.3
Excess tax benefit from share-based compensation	40.3	11.1
Other financing activities	(2.8)	(9.9)
Cash Used for Financing Activities	(232.4)	(300.0)
Effect of Exchange Rate Changes on Cash	10.7	(8.2)
Increase (Decrease) in Cash and Cash Items	55.8	(82.9)
Cash and Cash Items Beginning of Year	374.3	488.2
Cash and Cash Items End of Period	\$ 430.1	\$ 405.3

Supplemental Cash Flow Information

Significant noncash transactions:

Short-term borrowings associated with SAGA acquisition	\$	\$	54.6
Noncurrent liability related to the purchase of shares from noncontrolling interests			39.8

The accompanying notes are an integral part of these statements.

Table of Contents

AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Millions of dollars unless otherwise indicated, except for share data)

1. BASIS OF PRESENTATION AND MAJOR ACCOUNTING POLICIES

Refer to our 2010 Form 10-K for a description of major accounting policies. There have been no material changes to these accounting policies during the first nine months of 2011. Beginning in fiscal year 2011, we moved from a lattice-based option valuation model to a Black Scholes model to value stock option awards. The change in valuation models was not significant to our consolidated financial statements. Refer to Note 11, Share-Based Compensation, for further details on this change in accounting estimate.

The consolidated financial statements of Air Products and Chemicals, Inc. and its subsidiaries (we , our , us , the Company , Air Products , or registrant) included herein have been prepared by us, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. In our opinion, the accompanying statements reflect adjustments necessary to present fairly the financial position, results of operations, and cash flows for those periods indicated, and contain adequate disclosure to make the information presented not misleading. Adjustments included herein are of a normal, recurring nature unless otherwise disclosed in the Notes. The interim results for the periods indicated herein, however, do not reflect certain adjustments, such as the valuation of inventories on the LIFO cost basis, which can only be finally determined on an annual basis. The consolidated financial statements and related Notes included herein should be read in conjunction with the financial statements and Notes thereto included in our latest Form 10-K in order to fully understand the basis of presentation. Results of operations for interim periods are not necessarily indicative of the results of operations for a full year.

2. NEW ACCOUNTING GUIDANCE

Accounting Guidance Implemented

CONSOLIDATION OF VARIABLE INTEREST ENTITIES

In June 2009, the FASB issued authoritative guidance that amends previous guidance for determining whether an entity is a variable interest entity (VIE). It requires an enterprise to perform an analysis to determine whether the company's variable interests give it a controlling financial interest in a VIE. A company would be required to assess whether it has an implicit financial responsibility to ensure that a VIE operates as designed when determining whether it has the power to direct the activities of the VIE that most significantly impact the entity's economic performance. In addition, ongoing reassessments of whether an enterprise is the primary beneficiary of a VIE are required. This guidance was effective for us on 1 October 2010. The adoption of this guidance did not have a material impact on our consolidated financial statements.

MULTIPLE-DELIVERABLE REVENUE ARRANGEMENTS

In October 2009, the FASB issued authoritative guidance on multiple-deliverable revenue arrangements. This new guidance amends the existing criteria for separating consideration received in multiple-deliverable arrangements and requires that arrangement consideration be allocated at the inception of the arrangement to all deliverables based on their relative selling price. The guidance establishes a hierarchy for determining the selling price of a deliverable which is based on vendor-specific objective evidence, third-party evidence, or management estimates. Expanded disclosures related to multiple-deliverable revenue arrangements are also required. This guidance was effective for us on 1 October 2010. Upon adoption, the guidance was applied prospectively from the beginning of the fiscal year for new or materially modified arrangements. The adoption of this guidance did not have a material impact on our consolidated financial statements.

New Guidance to Be Implemented

STATEMENT OF COMPREHENSIVE INCOME

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In June 2011, the FASB issued authoritative guidance that amends previous guidance for the presentation of comprehensive income. It eliminates the current option to present other comprehensive income in the statement of changes in equity. Under this revised guidance, an entity will have the option to present the components of net income and other comprehensive income in either a single continuous statement of comprehensive income or in two separate but consecutive financial statements. The standard is effective for us beginning in the first quarter of fiscal year 2013. We are currently evaluating the alternatives for adopting the guidance, but we do not anticipate a material impact to our consolidated financial statements upon adoption.

Table of Contents

FAIR VALUE MEASUREMENTS

In May 2011, the FASB issued authoritative guidance that amends previous guidance for fair value measurement and disclosure requirements. The revised guidance changes certain fair value measurement principles, clarifies the application of existing fair value measurements and expands the disclosure requirements, particularly for Level 3 fair value measurements. This standard is effective for us beginning in the second quarter of fiscal year 2012. We are currently evaluating the impact of this guidance, but we do not anticipate a material impact to our consolidated financial statements upon adoption.

3. AIRGAS TRANSACTION

In February 2010, we commenced a tender offer to acquire all the outstanding common stock of Airgas, Inc. (Airgas), including the associated preferred stock purchase rights, for \$60.00 per share in cash, less any required withholding tax. The offer was subject to certain terms and conditions set forth in the Offer to Purchase dated 11 February 2010, as amended, including Airgas' redemption of the preferred stock purchase rights or such rights otherwise being inapplicable to our purchase of Airgas stock. Airgas, a Delaware company, is the largest U.S. distributor of industrial, medical, and specialty gases, and hard goods. On 9 December 2010, we increased the value of our tender offer to \$70.00 per share. At this price, the total value of the transaction would have been approximately \$7.8 billion, including \$6.1 billion of equity and \$1.7 billion of assumed debt. Based on a decision by the Delaware Chancery Court to uphold the decision of Airgas' Board of Directors to retain the preferred stock purchase rights, we withdrew our offer on 15 February 2011.

In connection with the tender offer, we had secured committed financing in the form of a \$6.7 billion term loan credit facility. Refer to Note 15, Debt, in our 2010 Form 10-K for additional information on this credit facility which would have expired 4 February 2011. On 3 February 2011, we entered into an amended and restated credit agreement providing for an amended \$6.7 billion term loan credit facility with a maturity date of 4 June 2011. The amended credit facility agreement contained the same covenants as the original agreement: one financial covenant, a maximum leverage ratio, and other affirmative and negative covenants, including restrictions on liens and certain subsidiary indebtedness. No additional underwriting fees were incurred in relation to the amended agreement. On 16 February 2011, in connection with the termination of the offer to purchase all outstanding shares of common stock of Airgas, the credit facility was terminated. No early termination penalties were incurred and all fees previously accrued and due under the credit facility were paid as of the date of termination.

Prior to the tender offer, we purchased approximately 1.5 million shares of Airgas stock for a total cost of \$69.6. This amount was recorded as an available-for-sale investment within other noncurrent assets on the consolidated balance sheet. On 16 February 2011, we sold the 1.5 million shares of Airgas stock for total proceeds of \$94.7 and recognized a gain of \$25.1 (\$15.9 after-tax, or \$.07 per share).

For the nine months ended 30 June 2011, a net loss of \$48.5 (\$31.6 after-tax, or \$.14 per share) was recognized related to this transaction. This amount is reflected separately on the consolidated income statement as Net loss on Airgas transaction and includes amortization of the fees related to the term loan credit facility, the gain on the sale of Airgas stock, and other acquisition-related costs. For the year ended 30 September 2010, \$96.0 (\$60.1 after-tax, or \$.28 per share) in expense was recognized in relation to this transaction. For the nine months ended 30 June 2011 and 2010, cash payments for the acquisition-related costs were \$156.2 and \$8.8, respectively. These payments are classified as operating activities on the consolidated statements of cash flows.

4. BUSINESS COMBINATIONS

In the second quarter of 2010, we entered into agreements that enabled us to acquire 100% of the outstanding shares of the French SAGA group (SAGA), which consists of SAGA, SAGA Medical, and SAGA Technologies. SAGA is an independent industrial gas provider in France with packaged gases, liquid/bulk, and medical businesses. The acquisition of SAGA supports the Merchant Gases segment's integration strategy by enhancing its market position in southwest and central France. SAGA revenues for calendar year 2009 were approximately \$25 million, or \$35.

Under the terms of these agreements, we purchased 51.47% of the shares of SAGA on 1 March 2010 for \$34.5 million or \$47.2 (\$25.0 net of cash acquired of \$22.2). The remaining shares were purchased on 30 November 2010 for a fixed price of \$44.8 million, or approximately \$62. At 30 September 2010, this structure was accounted for as a financing of the purchase of the remaining shares and reported within short-term borrowings on the consolidated balance sheet.

Table of Contents**5. INVENTORIES**

The components of inventories are as follows:

	30 June 2011	30 September 2010
Inventories at FIFO Cost		
Finished goods	\$452.1	\$405.3
Work in process	30.9	29.3
Raw materials and supplies	233.3	208.2
	716.3	642.8
Less: Excess of FIFO cost over LIFO cost	(76.7)	(71.2)
	\$639.6	\$571.6

FIFO cost approximates replacement cost. Our inventories have a high turnover, and as a result, there is little difference between the original cost of an item and its current replacement cost.

6. GOODWILL

Changes to the carrying amount of consolidated goodwill by segment for the nine months ended 30 June 2011 are as follows:

	30 September 2010	Acquisitions and Adjustments	Currency Translation	30 June 2011
Merchant Gases	\$595.7	\$	\$39.1	\$634.8
Tonnage Gases	15.5		1.0	16.5
Electronics and Performance Materials	303.4	2.0	12.4	317.8
	\$914.6	\$2.0	\$52.5	\$969.1

Goodwill is subject to impairment testing at least annually. In addition, goodwill is tested more frequently if a change in circumstances or the occurrence of events indicates that potential impairment exists.

7. FINANCIAL INSTRUMENTS**Currency Price Risk Management**

Our earnings, cash flows, and financial position are exposed to foreign currency risk from foreign currency denominated transactions and net investments in foreign operations. It is our policy to minimize the cash flow volatility to changes in currency exchange rates. This is accomplished by identifying and evaluating the risk that our cash flows will change in value due to changes in exchange rates and by determining the appropriate strategies necessary to manage such exposures. Our objective is to maintain economically balanced currency risk management strategies that provide adequate downside protection.

Forward Exchange Contracts

We enter into forward exchange contracts to reduce the cash flow exposure to foreign currency fluctuations associated with highly anticipated cash flows and certain firm commitments such as the purchase of plant and equipment. The maximum remaining term of any forward exchange contract currently outstanding at 30 June 2011 is 1.6 years. Forward exchange contracts are also used to hedge the value of investments in certain foreign subsidiaries and affiliates by creating a liability in a currency in which we have a net equity position. The primary currency pair in this portfolio of forward contracts is the Euro/U.S. Dollar.

In addition to the foreign exchange contracts that are designated as hedges, we also hedge foreign currency exposures utilizing forward exchange contracts that are not designated as hedges. These contracts are used to hedge foreign currency-denominated monetary assets and liabilities,

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primarily working capital. The primary objective of these forward contracts is to protect the value of foreign currency-denominated monetary assets and liabilities from the effects of volatility in foreign exchange rates that might occur prior to their receipt or settlement. This portfolio of forward exchange contracts is comprised of many different foreign currency pairs with a profile that changes from time to time depending on business activity and sourcing decisions.

Table of Contents

The table below summarizes our outstanding currency price risk management instruments:

	30 June 2011		30 September 2010	
	US\$	Years	US\$	Years
	Notional	Average Maturity	Notional	Average Maturity
Forward exchange contracts:				
Cash flow hedges	\$ 1,358.3	.4	\$ 1,605.5	.5
Net investment hedges	696.4	2.2	648.5	3.0
Hedges not designated	292.6	.1	373.6	.2
Total Forward Exchange Contracts	\$ 2,347.3	.9	\$ 2,627.6	1.1

In addition to the above, we use foreign currency denominated debt and qualifying intercompany loans to hedge the foreign currency exposures of our net investment in certain foreign affiliates. The designated foreign currency denominated debt at 30 June 2011 includes 724.7 million and NT\$975.0 million, and at 30 September 2010 includes 782.1 million and NT\$967.0 million. The designated intercompany loans were 437.0 million at 30 June 2011 and 30 September 2010.

Debt Portfolio Management

It is our policy to identify on a continuing basis the need for debt capital and evaluate the financial risks inherent in funding the Company with debt capital. Reflecting the result of this ongoing review, our debt portfolio and hedging program are managed with the objectives and intent to (1) reduce funding risk with respect to borrowings made by us to preserve our access to debt capital and provide debt capital as required for funding and liquidity purposes, and (2) manage the aggregate interest rate risk and the debt portfolio in accordance with certain debt management parameters.

Interest Rate Swap Contracts

We enter into interest rate swap contracts to change the fixed/variable interest rate mix of our debt portfolio in order to maintain the percentage of fixed- and variable-rate debt within the parameters set by management. In accordance with these parameters, the agreements are used to optimize interest rate risks and costs inherent in our debt portfolio. Our interest rate swap portfolio will generally consist of fixed to floating swaps and pre-issuance interest rate swap agreements to hedge the interest rate on anticipated fixed rate debt issuance. At 30 June 2011, the outstanding interest rate swaps were denominated in U.S. dollars and Euros. The maximum remaining hedged term of any interest rate swap designated as a cash flow hedge is 5.1 years. The notional amount of the interest rate swap agreements are equal to or less than the designated debt instrument being hedged. When interest rate swaps are used, the indices of the swap instruments and the debt to which they are designated are the same. It is our policy not to enter into any interest rate swap contracts which lever a move in interest rates on a greater than one-to-one basis.

Cross Currency Interest Rate Swap Contracts

We enter into cross currency interest rate swap contracts when risk management deems necessary. These contracts may entail both the exchange of fixed- and floating-rate interest payments periodically over the life of the agreement and the exchange of one currency for another currency at inception and at a specified future date. These contracts effectively convert the currency denomination of a debt instrument into another currency in which we have a net equity position while changing the interest rate characteristics of the instrument. The contracts are used to hedge long-term intercompany and third-party borrowing transactions and certain net investments in foreign operations. The current cross currency swap portfolio consists of a single fixed to fixed swap between U.S. dollars and British Pound Sterling.

Table of Contents

The following table summarizes our outstanding interest rate swaps and cross currency interest rate swaps:

	30 June 2011				30 September 2010			
	US\$ Notional	Pay %	Average Receive %	Years Average Maturity	US\$ Notional	Pay %	Average Receive %	Years Average Maturity
Interest rate swaps (fair value hedge)	\$595.2	LIBOR	3.40%	4.7	\$617.0	LIBOR	3.66%	3.8
Cross currency interest rate swaps (net investment hedge)	\$32.2	5.54%	5.50%	2.7	\$32.2	5.54%	5.48%	3.5
Interest rate swaps (cash flow hedge)	\$300.0	1.91%	LIBOR	5.1	\$			

The table below summarizes the fair value and balance sheet location of our outstanding derivatives:

	Balance Sheet Location	30 June 2011 Fair Value	30 September 2010 Fair Value	Balance Sheet Location	30 June 2011 Fair Value	30 September 2010 Fair Value
Derivatives Designated as Hedging Instruments:						
Forward exchange contracts	Other receivables	\$22.1	\$29.8	Accrued liabilities	\$45.5	\$22.3
Interest rate swap contracts	Other receivables	10.8	6.6	Accrued liabilities		1.3
Forward exchange contracts	Other noncurrent assets	18.7	38.7	Other noncurrent liabilities	.5	19.9
Interest rate swap contracts	Other noncurrent assets	18.3	33.1	Other noncurrent liabilities	3.1	2.4
Total Derivatives Designated as Hedging Instruments		\$69.9	\$108.2		\$49.1	\$45.9
Derivatives Not Designated as Hedging Instruments:						
Forward exchange contracts	Other receivables	\$ 2.3	\$ 6.2	Accrued liabilities	\$ 1.5	\$8.3
Total Derivatives		\$72.2	\$114.4		\$50.6	\$54.2

Refer to Note 8, Fair Value Measurements, which defines fair value, describes the method for measuring fair value, and provides additional disclosures regarding fair value measurements.

Table of Contents

The table below summarizes the gain or loss related to our cash flow hedges, fair value hedges, net investment hedges, and derivatives not designated as hedging instruments.

	Three Months Ended 30 June							
	Forward		Foreign Currency		Other ^(A)		Total	
	Exchange Contracts		Debt					
	2011	2010	2011	2010	2011	2010	2011	2010
Cash Flow Hedges:								
Net (gain) loss recognized in OCI (effective portion)	\$ (6.1)	\$ 16.0	\$	\$	\$.8	\$	\$ (5.3)	\$ 16.0
Net gain (loss) reclassified from OCI to sales/cost of sales (effective portion)	(1.3)	(.7)					(1.3)	(.7)
Net gain (loss) reclassified from OCI to other (income) expense (effective portion)	6.7	(15.1)					6.7	(15.1)
Net gain (loss) reclassified from OCI to other (income) expense (ineffective portion)	(.5)	.1					(.5)	.1
Fair Value Hedges:								
Net (gain) loss recognized in other (income) expense ^(B)	\$	\$	\$	\$	\$ (8.4)	\$ (10.8)	\$ (8.4)	\$ (10.8)
Net Investment Hedges:								
Net (gain) loss recognized in OCI	\$ 8.0	\$ (53.7)	\$ 30.5	\$ (117.0)	\$.2	\$ (.4)	\$ 38.7	\$ (171.1)
Derivatives Not Designated as Hedging Instruments:								
Net (gain) loss recognized in other (income) expense ^(C)	\$ 1.4	\$ (.4)	\$	\$	\$	\$	\$ 1.4	\$ (.4)

	Nine Months Ended 30 June							
	Forward		Foreign Currency		Other ^(A)		Total	
	Exchange Contracts		Debt					
	2011	2010	2011	2010	2011	2010	2011	2010
Cash Flow Hedges:								
Net (gain) loss recognized in OCI (effective portion)	\$ (8.5)	\$ 25.1	\$	\$	\$.8	\$.2	\$ (7.7)	\$ 25.3
Net gain (loss) reclassified from OCI to sales/cost of sales (effective portion)	(7.4)	(5.6)				2.0	(7.4)	(3.6)
Net gain (loss) reclassified from OCI to other (income) expense (effective portion)	7.5	(19.8)					7.5	(19.8)
Net (loss) reclassified from OCI to other (income) expense (ineffective portion)	(.6)	(.1)					(.6)	(.1)
Fair Value Hedges:								
Net (gain) loss recognized in other (income) expense ^(B)	\$	\$	\$	\$	\$ 12.8	\$ (10.9)	\$ 12.8	\$ (10.9)
Net Investment Hedges:								
Net (gain) loss recognized in OCI	\$ 22.3	\$ (89.3)	\$ 84.6	\$ (236.0)	\$.5	\$ (1.3)	\$ 107.4	\$ (326.6)
Derivatives Not Designated as Hedging Instruments:								
Net (gain) loss recognized in other (income) expense ^(C)	\$ 2.1	\$ (3.9)	\$	\$	\$	\$	\$ 2.1	\$ (3.9)

^(A) Other includes the impact on other comprehensive income (OCI) and earnings related to interest rate swaps.

^(B) The impact of the fair value hedges noted above was largely offset by gains and losses resulting from the impact of changes in related interest rates on recognized outstanding debt.

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^(C) The impact of the non-designated hedges noted above was largely offset by gains and losses, respectively, resulting from the impact of changes in exchange rates on recognized assets and liabilities denominated in nonfunctional currencies.

The amount of estimated cash flow hedges' unrealized gains and losses which are expected to be reclassified to earnings in the next twelve months is not material.

Table of Contents

Credit Risk-Related Contingent Features

Certain derivative instruments are executed under agreements that require us to maintain a minimum credit rating with both Standard & Poor's and Moody's. If our credit rating falls below this threshold, the counterparty to the derivative instruments has the right to request full collateralization on the derivatives' net liability position. The net liability position of derivatives with credit risk-related contingent features was \$21.3 as of 30 June 2011 and \$4.2 as of 30 September 2010. Because our current credit rating is above the various pre-established thresholds, no collateral has been posted on these liability positions.

Counterparty Credit Risk Management

We execute all derivative transactions with counterparties that are highly rated financial institutions all of which are investment grade at this time. Some of our underlying derivative agreements give us the right to require the institution to post collateral if its credit rating falls below the pre-established thresholds with Standard & Poor's or Moody's. These are the same agreements referenced in Credit Risk-Related Contingent Features above. The collateral that the counterparties would be required to post was \$29.0 as of 30 June 2011 and \$52.2 as of 30 September 2010. No financial institution is required to post collateral at this time, as all have credit ratings at or above the threshold.

8. FAIR VALUE MEASUREMENTS

Fair value is defined as an exit price (i.e., 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 methods and assumptions used to measure the fair value of financial instruments are as follows:

Derivatives

The fair value of our interest rate swap agreements and foreign exchange contracts are quantified using the income approach and are based on estimates using standard pricing models. These models take into account the value of future cash flows as of the balance sheet date, discounted to a present value using discount factors that match both the time to maturity and currency of the underlying instruments. The computation of the fair values of these instruments is generally performed by the Company. These standard pricing models utilize inputs which are derived from or corroborated by observable market data such as interest rate yield curves and currency spot and forward rates. In addition, on an ongoing basis, we randomly test a subset of our valuations against valuations received from the transaction's counterparty to validate the accuracy of our standard pricing models.

Refer to Note 7, Financial Instruments, for a description of derivative instruments, including details on the balance sheet line item classifications.

Available-for-Sale Securities

The fair value of available-for-sale securities is based on a market approach, specifically quoted market prices in publicly traded companies from the New York Stock Exchange and NASDAQ. These investments are reported within other noncurrent assets on the consolidated balance sheet, with holding gains and losses recorded to other comprehensive income, net of tax, within total equity.

Long-term Debt

The fair value of our debt is based on estimates using standard pricing models that take into account the value of future cash flows as of the balance sheet date, discounted to a present value using discount factors that match both the time to maturity and currency of the underlying instruments. These standard valuation models utilize observable market data such as interest rate yield curves and currency spot rates. The computation of the fair value of these instruments is generally performed by the Company.

Other Liabilities

Other liabilities include the obligation to purchase 25% of the remaining shares of CryoService Limited (CSL). CSL is not publically traded and therefore, no observable market exists for the shares. The fair value of the outstanding liability was determined using an internally developed valuation model that was based on a multiple of earnings formula. The liability is reported in accrued liabilities on the consolidated balance sheet.

Table of Contents

The carrying values and fair values of financial instruments were as follows:

	30 June 2011		30 September 2010	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Assets				
Derivatives				
Foreign exchange contracts	\$43.1	\$43.1	\$74.7	\$74.7
Interest rate swap contracts	29.1	29.1	39.7	39.7
Available-for-sale securities				
Airgas investment			102.5	102.5
Other investments			1.1	1.1
Liabilities				
Derivatives				
Foreign exchange contracts	\$47.5	\$47.5	\$50.5	\$50.5
Interest rate swap contracts	3.1	3.1	3.7	3.7
Long-term debt, including current portion	4,067.3	4,266.5	3,842.3	4,146.4
Other liabilities	50.8	50.8	42.0	42.0

The carrying amounts reported in the balance sheet for cash and cash items, trade receivables, payables and accrued liabilities, accrued income taxes, and short-term borrowings approximate fair value due to the short-term nature of these instruments. Accordingly, these items have been excluded from the above table.

The fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three broad levels as follows:

- Level 1 Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 Inputs that are observable for the asset or liability, either directly or indirectly through market corroboration, for substantially the full term of the asset or liability.
- Level 3 Inputs that are unobservable for the asset or liability based on our own assumptions (about the assumptions market participants would use in pricing the asset or liability).

The following table summarizes assets and liabilities measured at fair value on a recurring basis in the consolidated balance sheets:

	30 June 2011				30 September 2010			
	Total	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3
Assets at Fair Value								
Derivatives								
Foreign exchange contracts	\$ 43.1	\$	\$ 43.1	\$	\$ 74.7	\$	\$ 74.7	\$
Interest rate swap contracts	29.1		29.1		39.7		39.7	
Available-for-sale securities								
Airgas investment					102.5	102.5		
Other investments					1.1	1.1		
Total Assets at Fair Value	\$ 72.2	\$	\$ 72.2	\$	\$ 218.0	\$ 103.6	\$ 114.4	\$
Liabilities at Fair Value								
Derivatives								
Foreign exchange contracts	\$ 47.5	\$	\$ 47.5	\$	\$ 50.5	\$	\$ 50.5	\$
Interest rate swap contracts	3.1		3.1		3.7		3.7	
Other liabilities	50.8			50.8	42.0			42.0
Total Liabilities at Fair Value	\$ 101.4	\$	\$ 50.6	\$ 50.8	\$ 96.2	\$	\$ 54.2	\$ 42.0

Refer to Note 1, Major Accounting Policies, in our 2010 Form 10-K and Note 7, Financial Instruments, in this quarterly filing for additional information on our accounting and reporting of the fair value of financial instruments.

Table of Contents

Changes in the fair value of other liabilities, valued using significant unobservable inputs (Level 3), are presented below:

Balance at 30 September 2010	\$ 42.0
Expense included in interest expense	.5
Adjustment to initial estimate (see FN 14)	6.1
Balance at 31 December 2010	\$ 48.6
Expense included in interest expense	1.7
Currency translation adjustment	1.1
Balance at 31 March 2011	\$ 51.4
Income included in interest expense	(.7)
Currency translation adjustment	.1
Balance at 30 June 2011	\$ 50.8

9. RETIREMENT BENEFITS

The components of net pension cost for the defined benefit pension plans and other postretirement benefit cost for the three and nine months ended 30 June 2011 and 2010 were as follows:

	Pension Benefits				Other Benefits	
	2011		2010		2011	2010
Three Months Ended 30 June	U.S.	International	U.S.	International		
Service cost	\$10.9	\$ 7.5	\$10.6	\$ 5.7	\$1.4	\$ 1.2
Interest cost	30.7	16.3	30.9	14.3	0.8	1.1
Expected return on plan assets	(44.9)	(17.3)	(41.1)	(15.3)		
Prior service cost amortization	.6	.2	.7	.1		
Actuarial loss amortization	16.0	7.7	11.7	4.7	1.0	.7
Settlement and curtailment charges			5.8	.5		
Special termination benefits		.3	(.7)			
Other		.8		.2		
Net periodic benefit cost	\$ 13.3	\$ 15.5	\$ 17.9	\$ 10.2	\$ 3.2	\$ 3.0

	Pension Benefits				Other Benefits	
	2011		2010		2011	2010
Nine Months Ended 30 June	U.S.	International	U.S.	International		
Service cost	\$32.7	\$ 22.0	\$31.8	\$ 17.9	\$ 4.2	\$ 3.6
Interest cost	92.2	48.0	92.7	45.3	2.4	3.3
Expected return on plan assets	(134.7)	(50.9)	(123.3)	(48.2)		
Prior service cost amortization	1.8	.6	2.1	.5		
Actuarial loss amortization	48.0	23.3	35.1	14.7	3.0	2.1
Settlement and curtailment charges			5.8	.5		
Special termination benefits		.3	(.7)	3.5		
Other		1.7		2.1		
Net periodic benefit cost	\$ 40.0					