

GRAFTECH INTERNATIONAL LTD

Form 10-Q

July 29, 2015

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

for the quarterly period ended June 30, 2015

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: 1-13888

GRAFTECH INTERNATIONAL LTD.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of  
incorporation or organization)

27-2496053

(I.R.S. Employer  
Identification Number)

Suite 300 Park Center I  
6100 Oak Tree Boulevard  
Independence, OH

44131  
(Zip code)

(Address of principal executive offices)

Registrant's telephone number, including area code: (216) 676-2000

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

Large Accelerated Filer ☐

Accelerated Filer ☐

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Non-Accelerated Filer ☐

Smaller Reporting Company ☐

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

As of July 17, 2015, 137,302,959 shares of common stock, par value \$.01 per share, were outstanding.

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## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

## GRAFTECH INTERNATIONAL LTD. AND SUBSIDIARIES

## CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except share data)

(Unaudited)

	As of December 31, 2014	As of June 30, 2015	
<b>ASSETS</b>			
Current assets:			
Cash and cash equivalents	\$ 17,550	\$ 14,505	
Accounts and notes receivable, net of allowance for doubtful accounts of \$7,471 as of December 31, 2014 and \$6,459 as of June 30, 2015	162,919	121,686	
Inventories	382,903	375,633	
Prepaid expenses and other current assets	81,623	77,952	
Total current assets	644,995	589,776	
Property, plant and equipment	1,500,821	1,477,360	
Less: accumulated depreciation	846,781	842,689	
Net property, plant and equipment	654,040	634,671	
Deferred income taxes	16,819	17,116	
Goodwill	420,129	384,432	
Other assets	97,822	86,979	
Total assets	\$ 1,833,805	\$ 1,712,974	
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>			
Current liabilities:			
Accounts payable	\$ 86,409	\$ 72,136	
Short-term debt	188,104	199,215	
Accrued income and other taxes	24,506	20,412	
Rationalizations	9,563	7,399	
Other accrued liabilities	43,319	31,252	
Total current liabilities	351,901	330,414	
Long-term debt	341,615	349,335	
Other long-term obligations	107,566	99,512	
Deferred income taxes	28,197	24,237	
Contingencies – Note 12			
Stockholders' equity:			
Preferred stock, par value \$.01, 10,000,000 shares authorized, none issued	—	—	
Common stock, par value \$.01, 225,000,000 shares authorized, 152,821,011 shares issued as of December 31, 2014 and 153,225,065 shares issued as of June 30, 2015	1,528	1,532	
Additional paid-in capital	1,825,880	1,829,391	
Accumulated other comprehensive loss	(336,524)	(357,733)	)
Retained earnings (deficit)	(245,751)	(324,176)	)
Less: cost of common stock held in treasury, 15,922,729 shares as of December 31, 2014 and 15,870,143 shares as of June 30, 2015	(239,811)	(238,881)	)
Less: common stock held in employee benefit and compensation trusts, 80,967 shares as of December 31, 2014 and 69,244 shares as of June 30, 2015	(796)	(657)	)

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Total stockholders' equity	1,004,526	909,476
Total liabilities and stockholders' equity	\$1,833,805	\$1,712,974
See accompanying Notes to Consolidated Financial Statements		

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GRAFTECH INTERNATIONAL LTD. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME  
(Dollars in thousands, except per share amounts)  
(Unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2014	2015	2014	2015
<b>CONSOLIDATED STATEMENTS OF OPERATIONS</b>				
Net sales	\$284,184	\$165,122	\$564,975	\$372,333
Cost of sales	266,231	149,183	521,328	335,631
Gross profit	17,953	15,939	43,647	36,702
Research and development	2,903	1,914	5,673	4,345
Selling and administrative expenses	32,137	25,253	62,044	51,543
Rationalizations	831	1,769	917	4,263
Impairments	121,570	—	121,570	35,381
Operating loss	(139,488 )	(12,997 )	(146,557 )	(58,830 )
Other expense (income), net	(41 )	699	753	1,092
Interest expense	9,155	9,195	18,154	18,116
Interest income	(55 )	(273 )	(113 )	(346 )
Loss before provision for income taxes	(148,547 )	(22,618 )	(165,351 )	(77,692 )
Provision for income taxes	6,886	199	1,599	733
Net loss	\$(155,433 )	\$(22,817 )	\$(166,950 )	\$(78,425 )
Basic loss per common share:				
Net loss per share	\$(1.14 )	\$(0.17 )	\$(1.23 )	\$(0.57 )
Weighted average common shares outstanding	135,963	137,252	135,713	137,113
Diluted loss per common share:				
Net loss per share	\$(1.14 )	\$(0.17 )	\$(1.23 )	\$(0.57 )
Weighted average common shares outstanding	135,963	137,252	135,713	137,113
<b>STATEMENTS OF COMPREHENSIVE INCOME</b>				
Net loss	\$(155,433 )	\$(22,817 )	\$(166,950 )	\$(78,425 )
Other comprehensive income:				
Foreign currency translation adjustments	(240 )	7,515	2,147	(22,096 )
Commodities and foreign currency derivatives and other, net of tax of (\$169), \$76, (\$53) and (\$78), respectively	479	42	164	887
Other comprehensive income (loss), net of tax:	239	7,557	2,311	(21,209 )
Comprehensive loss	\$(155,194 )	\$(15,260 )	\$(164,639 )	\$(99,634 )

See accompanying Notes to Consolidated Financial Statements

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CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)

(Unaudited)

	For the Six Months Ended June 30,	
	2014	2015
Cash flow from operating activities:		
Net loss	\$(166,950	) \$(78,425 )
Adjustments to reconcile net income to cash provided by operations:		
Depreciation and amortization	66,507	39,384
Impairments	121,570	35,381
Deferred income tax provision	(1,724	) (4,947 )
Post-retirement and pension plan changes	3,093	2,252
Stock-based compensation	2,752	2,628
Interest expense	7,471	7,699
Other charges, net	2,783	(1,321 )
Decrease in working capital*	30,416	30,395
Increase in long-term assets and liabilities	(10,018	) (8,826 )
Net cash provided by operating activities	55,900	24,220
Cash flow from investing activities:		
Capital expenditures	(46,464	) (25,620 )
Proceeds from the sale of assets	2,523	638
Payments for derivative instruments	(194	) (7,804 )
Insurance recoveries	2,834	—
Net cash used in investing activities	(41,301	) (32,786 )
Cash flow from financing activities:		
Short-term debt, net	(1,019	) 4,506
Revolving Facility borrowings	209,000	74,000
Revolving Facility reductions	(205,000	) (66,000 )
Principal payments on long-term debt	(126	) (67 )
Supply chain financing	(9,455	) —
Proceeds from exercise of stock options	2,813	—
Purchase of treasury shares	(435	) (63 )
Revolving Facility refinancing fees	(2,636	) (2,722 )
Other	918	(2,850 )
Net cash (used in) provided by financing activities	(5,940	) 6,804
Net increase (decrease) in cash and cash equivalents	8,659	(1,762 )
Effect of exchange rate changes on cash and cash equivalents	181	(1,283 )
Cash and cash equivalents at beginning of period	11,888	17,550
Cash and cash equivalents at end of period	\$20,728	\$14,505

\* Net change in working capital due to the following components:

Change in current assets:		
Accounts and notes receivable, net	\$22,158	\$34,858
Inventories	42,298	3,274
Prepaid expenses and other current assets	(18,660	) 6,238
Decrease in accounts payable and accruals	(284	) (11,806 )
Rationalizations	(15,076	) (2,183 )

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(Decrease) increase in interest payable	(20	) 14
Decrease in working capital	\$ 30,416	\$ 30,395

See accompanying Notes to Consolidated Financial Statements

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GRAFTECH INTERNATIONAL LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(1) Organization and Summary of Significant Accounting Policies

A. Organization

GrafTech International Ltd. (the "Company") is one of the world's largest manufacturers and providers of high quality synthetic and natural graphite and carbon based products. References herein to "GTI," "we," "our," or "us" refer collectively to GrafTech International Ltd. and its subsidiaries. We have seven major product categories: graphite electrodes, refractory products, needle coke products, advanced electronics technologies, advanced graphite materials, advanced composite materials and advanced materials, which are reported in the following segments:

Industrial Materials includes graphite electrodes, refractory products, and needle coke products, and primarily serves the steel industry.

Engineered Solutions includes advanced electronics technologies, advanced graphite materials, advanced composite materials and advanced materials, and provides primary and specialty products to the advanced electronics, industrial, energy, transportation and defense industries.

B. Basis of Presentation

The interim Consolidated Financial Statements are unaudited; however, in the opinion of management, they have been prepared in accordance with Rule 10-01 of Regulation S-X and in accordance with accounting principles generally accepted in the United States of America ("GAAP"). The December 31, 2014 financial position data included herein was derived from the audited consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2014 (the "Annual Report") but does not include all disclosures required by GAAP. These interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements, including the accompanying notes, contained in the Annual Report.

The unaudited consolidated financial statements reflect all adjustments (all of which are of a normal, recurring nature) which management considers necessary for a fair statement of financial position, results of operations, comprehensive income and cash flows for the interim period presented. The results for the interim periods are not necessarily indicative of results which may be expected for any other interim period or for the full year.

C. New Accounting Standards

In May 2014, FASB issued ASU No. 2014-09, Revenue from Contracts with Customers. This ASU supersedes the revenue recognition requirements in Accounting Standards Codification 605—Revenue Recognition and most industry-specific guidance throughout the Codification. This ASU requires that an entity recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This ASU is supposed to be effective for fiscal years beginning after December 15, 2016, and for interim periods within those fiscal years. On July 9, 2015, the FASB deferred the effective date to fiscal years beginning after December 15, 2017. We are in the process of assessing the impact of the adoption of ASU 2014-09 on the Company's financial position, results of operations and cash flows. On April 7, 2015, FASB issued ASU 2015-3, Simplifying the Presentation of Debt Issuance Costs, which requires debt issuance costs to be presented in the balance sheet as a direct deduction from the carrying value of the associated debt liability. The standard is effective for financial statements issued for fiscal years beginning after December 15, 2015. The Company had \$9.7 million and \$11.3 million of capitalized bank fees included within "Other Assets" on our consolidated balance sheets as of December 31, 2014 and June 30, 2015, respectively.

(2) Pending Preferred Share Issuance and Tender Offer

Preferred Stock

On May 4, 2015, the Company entered into an Investment Agreement (the "Investment Agreement") with BCP IV GrafTech Holdings LP, an affiliate of Brookfield Capital Partners Ltd. ("Brookfield"), pursuant to which the Company agreed to issue and sell and Brookfield agreed to purchase and pay for: (i) shares of a new Series A Convertible Preferred Stock, par value \$0.01 per share (the "Series A Preferred Stock") in an amount equal to 19.9% of the



PART I (CONT'D)

GRAFTECH INTERNATIONAL LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Company's outstanding common stock (the "Series A Preferred Shares") and (ii) shares of a new Series B Convertible Preferred Stock, par value \$0.01 per share (the "Series B Preferred Stock," and, together with the Series A Preferred Stock, the "Preferred Stock"), in an amount equal to 150,000 less the number of Series A Preferred Shares, for an aggregate purchase price of \$150,000,000 in cash (the "Purchase Price").

The closing of the purchase and sale of the Preferred Stock (the "Closing") is expected to occur upon the satisfaction of customary closing conditions set forth in the Investment Agreement and the satisfaction of any other applicable regulatory approval requirements.

Pursuant to the Investment Agreement, the Company is required to reimburse Brookfield for its reasonable, out-of-pocket fees and expenses (including the reasonable fees and expenses of legal counsel, accountants, investment bankers, brokers, or other representatives or consultants) up to \$500,000 incurred in connection with the transaction. The proceeds from the sale of the Preferred Stock will be used by the Company, along with its other cash and borrowing resources, to repay the Company's senior subordinated notes due to mature in November 2015.

Upon issuance, the Series A Preferred Stock will be immediately convertible, at Brookfield's option, into shares of common stock of the Company, at a conversion price of \$5.00 per common share, subject to customary anti-dilution adjustments. Each share of the Series B Preferred Stock will automatically convert into one share of Series A Preferred Stock upon approval by the Company's stockholders of such conversion in accordance with New York Stock Exchange requirements (the "Stockholder Approval"). The Company has agreed to seek the Stockholder Approval at the Company's 2015 annual stockholders meeting.

The Preferred Stock will be entitled to an annual dividend at the rate of 7.0% prior to any dividend or distribution with respect to any of the Company's capital stock junior to the Preferred Stock, which will be due and payable quarterly in arrears in cash. Dividends will be cumulative and will accrue until paid. If the Company fails to make timely dividend payments, the dividend rate would increase to 8% per annum until such time as all accrued but unpaid dividends have been paid in full. The Preferred Stock will have a liquidation preference equal to the greater of (x) \$1,000 per share, plus all accrued and unpaid dividends thereon, whether or not declared and (y) the amount that the holders of the Preferred Stock would have received had they converted the Preferred Stock into shares of common stock (or Series A Preferred Stock in the case of Series B Preferred Stock) immediately prior to the time of liquidation. The Preferred Stock will rank junior to the Company's existing and future indebtedness. The Series A Preferred Stock will have certain mandatory redemption rights at the holders' option following the seventh anniversary of the issue date and certain redemption rights at the option of the Company following the fourth anniversary of the issue date if the daily volume weighted average price of the Company's common stock equals or exceeds 175.0% of the conversion price for at least 40 trading days during a period of 60 consecutive trading days, in each instance at a redemption price per share equal to \$1,000 per share plus all accrued and unpaid dividends thereon, whether or not declared. The Series B Preferred Stock has a mandatory redemption right at the holders' option if the Stockholder Approval is not obtained by a specified date. The holders of the Preferred Stock also have the right, upon the occurrence of a change of control (other than one for which such holders have a repurchase right under the Investment Agreement), to require the Company to repurchase all or any portion of such holder's shares of Preferred Stock, at a make-whole premium.

The holders of the Preferred Stock will be entitled to vote as a class on matters adversely affecting the Preferred Stock and, subject to certain ownership thresholds, on the election of designated board nominees, and the holders of the Series A Preferred Stock will be entitled to vote together with the holders of common stock, as a single class, on an as converted basis, on other matters. So long as 25% of the originally issued shares of Series A Preferred Stock is outstanding, holders of a majority of the Preferred Stock are entitled to veto rights over issuances of senior or parity securities and changes to the certificate of incorporation of the Company that are adverse to the Preferred Stock. We recorded \$2.9 million of issuance costs related to the Preferred Stock transaction as of June 30, 2015 in Prepaid and other current assets on the balance sheet, of which \$2.7 million were paid in cash and included in the Cash Flow

from Financing section of the Statement of Cash flows.

If the convertible preferred stock is issued, it would trigger acceleration of vesting of certain equity awards, performance awards at 100%, accelerated payment of certain awards and deferred compensation. If at least the minimum number of shares is purchased in the tender offer, it would constitute a change in control (as defined in our Credit Agreement) of the Company. As a result, the administrative agent, or lenders having more than 50% of the term loans, revolving exposures and unused commitments under our Credit Agreement may terminate the commitments

PART I (CONT'D)

GRAFTECH INTERNATIONAL LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

under the Credit Agreement and declare the loans thereunder then outstanding to be due and payable in whole (or in part). In addition, if more than 35% of the then outstanding shares are purchased in the tender offer, it would constitute a change in control (as defined in the indenture for the Senior Notes) of the Company. If certain downgrades of the ratings of the Senior Notes as specified in the indenture occur subsequent to the change in control, the Company will be required to offer to repurchase any or all of the Senior Notes at a repurchase price equal to 101% of the aggregate principal amount of the Senior Notes, plus any accrued and unpaid interest. Finally, if, prior to maturity or redemption, a change in control (as defined in the Senior Subordinated Notes) of the Company occurs, the holders of a majority of the Senior Subordinated Notes may, by written notice to the Company, declare the principal amount then outstanding under all (but not less than all) of the Senior Subordinated Notes to be immediately due and payable. If either the Credit Agreement or the Senior Subordinated Notes were accelerated, that may result in events of default in other agreements, including the indenture for the Senior Notes, which would permit the counterparties to such agreements to terminate those agreements and accelerate amounts that may be due thereunder. In addition, such transactions could impact the cash flows, ability to utilize net operating losses, earnings per share and other financial metrics and could result in litigation. We intend to obtain waivers relating to the change in control provisions in our Credit Agreement, however, there is no assurance we will be able to obtain such waivers.

Merger Agreement

On May 17, 2015, the Company entered into an Agreement and Plan of Merger (the "Merger Agreement") with BCP IV GrafTech Holdings LP, a Delaware limited partnership ("Parent"), and Athena Acquisition Subsidiary Inc., a Delaware corporation and a wholly owned subsidiary of Parent ("Acquisition Sub"), pursuant to which, among other things, Parent has agreed to make a cash tender offer (the "Offer") to purchase any and all of the outstanding shares of the Company's common stock, par value \$0.01 per share (the "Shares"), at a purchase price of \$5.05 per Share in cash (the "Offer Price"). Parent and Acquisition Sub are indirect wholly owned subsidiaries of Brookfield.

The Offer commenced on May 26, 2015. The Offer's initial term was extended in accordance with the Merger Agreement and expired at midnight, New York Time, on July 28, 2015. The Offer was again extended in accordance with the Merger Agreement for an additional ten business days to allow for regulatory approvals. The Offer is to expire at midnight, New York Time, on August 13, 2015. The Offer is subject to the condition that prior to the expiration of the Offer, there have been validly tendered and not withdrawn, a number of Shares that, together with the Shares then owned by Brookfield and its controlled affiliates (including Shares issuable upon conversion of the Preferred Stock) represents at least 30% of the then outstanding Shares (the "Minimum Condition").

Pursuant to the Merger Agreement, if Shares validly tendered and not withdrawn in the Offer, together with the Shares then owned by Brookfield and its controlled affiliates (including Shares issuable upon conversion of the Preferred Stock, represent at least 80% of the then outstanding Shares plus the Shares issuable upon conversion of the Preferred Stock (the "Merger Condition"), Parent will transfer the Preferred Stock held by Parent to Acquisition Sub, Acquisition Sub (instead of Parent) will accept the Shares for purchase in the Offer and Acquisition Sub will merge with and into the Company, the separate corporate existence of Acquisition Sub will cease and the Company will continue as the surviving corporation and a wholly owned subsidiary of Parent (the "Merger"). If the Merger Condition is satisfied, each Share that is not tendered and accepted pursuant to the Offer (other than cancelled shares, dissenting shares and shares held by the Company's subsidiaries or Parent's subsidiaries (other than Acquisition Sub)) will thereupon be cancelled and converted into the right to receive cash consideration in an amount equal to the Offer Price. The Merger Agreement contemplates that the Merger would be effected pursuant to Section 251(h) of the General Corporation Law of the State of Delaware (the "DGCL") pursuant to which no stockholder vote will be required to consummate the Merger. If the Company terminates the Merger Agreement to enter into an agreement for a superior proposal (as defined in the Merger Agreement), the Company would be required to pay a designee of the Parent a \$20 million termination fee.



## PART I (CONT'D)

## GRAFTECH INTERNATIONAL LTD. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

## (3) Rationalizations and Impairments

Throughout 2013, 2014 and 2015 the Company undertook rationalization plans in order to streamline our organization and lower our production costs. The total rationalization and related charges incurred during the three and six months ended June 30, 2014 and 2015 are as follows:

All Plans	For the Three Months Ended June 30, 2014				For the Three Months Ended June 30, 2015			
	Industrial Materials Segment	Engineered Solutions Segment	Corp, R&D and Other	Total	Industrial Materials Segment	Engineered Solutions Segment	Corp, R&D and Other	Total
(Dollars in thousands)								
Recorded in Cost of Sales								
Accelerated depreciation	\$3,832	\$413	\$—	\$4,245	\$—	\$—	\$—	\$—
Inventory loss	(148 )	11,057	—	10,909	—	144	—	144
Fixed asset write-offs and other	4,403	131	—	4,534	413	1,072	—	1,485
Recorded in Research and Development								
Accelerated depreciation	—	—	—	—	—	—	319	319
Recorded in Selling and General Administrative								
Other	53	—	—	53	400	292	(276 )	416
Recorded in Rationalizations								
Severance and related costs	304	—	—	304	104	1,641	(130 )	1,615
Contract terminations	527	—	—	527	—	154	—	154
Total	\$8,971	\$11,601	\$—	\$20,572	\$917	\$3,303	\$(87 )	\$4,133

In the three months ended June 30, 2015, in connection with our rationalization initiatives, two sites, located respectively in Salvador, Brazil and in Pennsylvania, United States, substantially completed their decommissioning efforts and met the criteria for assets held for sale. Because the carrying value of the sites did not exceed their estimated fair value, no additional impairment was recorded. As of June 30, 2015, the sites held for sale represent \$1.7 million of assets reported under "Property, plant and equipment" and \$0.5 million of liabilities, reported under "Other accrued liabilities".

## PART I (CONT'D)

## GRAFTECH INTERNATIONAL LTD. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

All Plans	For the Six Months Ended June 30, 2014				For the Six Months Ended June 30, 2015			
	Industrial Materials Segment	Engineered Solutions Segment	Corp, R&D and Other	Total	Industrial Materials Segment	Engineered Solutions Segment	Corp, R&D and Other	Total
(Dollars in thousands)								
Recorded in Cost of Sales								
Accelerated depreciation	\$20,852	\$826	\$—	\$21,678	\$432	\$—	\$—	\$432
Inventory loss	667	11,048	—	11,715	(61	) 947	—	886
Fixed asset write-offs and other	3,909	131	—	4,040	1,655	973	—	2,628
Recorded in Research and Development								
Accelerated depreciation	—	—	—	—	—	—	940	940
Recorded in Selling and General Administrative								
Other	78	—	—	78	400	295	790	1,485
Recorded in Rationalizations								
Severance and related costs	418	(28	) —	390	157	4,006	(130	) 4,033
Contract terminations	528	—	—	527	25	204	—	229
Total	\$26,452	\$11,977	\$—	\$38,428	\$2,608	\$6,425	\$1,600	\$10,633

## 2013 Industrial Materials Rationalization

On October 31, 2013, we announced a global initiative to reduce our Industrial Materials segment's cost base and improve our competitive position. As part of this initiative, we ceased production at our two highest cost graphite electrode plants, located in Brazil and South Africa, as well as a machine shop in Russia. Our graphite electrode capacity was reduced by approximately 60,000 metric tons as a result of these actions. In parallel, we adopted measures for reductions in overhead and related corporate operations. These actions and measures reduced global headcount by approximately 600 people, or approximately 20 percent of our global workforce. These actions were substantially completed during the first half of 2014.

## 2013 Engineered Solutions Rationalization

In order to optimize our Engineered Solutions platform and improve our cost structure, we also initiated actions to centralize certain operations and reduce overhead in our Engineered Solutions segment. These actions reduced global headcount by approximately 40 people and were substantially completed during 2014.





## PART I (CONT'D)

## GRAFTECH INTERNATIONAL LTD. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

## Total 2013 Rationalization Initiatives Impact to Financial Results

Charges incurred related to the 2013 rationalization initiatives for the six months ended June 30, 2014 and June 30, 2015 are as follows:

2013 Plans	For the Three Months Ended June 30, 2014				For the Three Months Ended June 30, 2015			
	Industrial Materials Segment	Engineered Solutions Segment	Corp, R&D and Other	Total	Industrial Materials Segment	Engineered Solutions Segment	Corp, R&D and Other	Total
(Dollars in thousands)								
Recorded in Cost of Sales								
Accelerated depreciation	\$3,832	\$413	\$—	\$4,245	\$—	\$—	\$—	\$—
Inventory loss	(148	) 496	—	348	—	—	—	—
Fixed asset write-offs and other	4,403	131	—	4,534	413	249	—	662
Recorded in Selling and General Administrative								
Other	52	—	—	52	—	—	—	—
Recorded in Rationalizations								
Severance and related costs	304	—	—	304	10	146	—	156
Contract terminations	528	—	—	528	—	—	—	—
Total	\$8,971	\$1,040	\$—	\$10,011	\$423	\$395	\$—	\$818
2013 Plans	For the Six Months Ended June 30, 2014				For the Six Months Ended June 30, 2015			
	Industrial Materials Segment	Engineered Solutions Segment	Corp, R&D and Other	Total	Industrial Materials Segment	Engineered Solutions Segment	Corp, R&D and Other	Total
(Dollars in thousands)								
Recorded in Cost of Sales								
Accelerated depreciation	\$20,852	\$826	\$—	\$21,678	\$432	\$—	\$—	\$432
Inventory loss	667	486	—	1,153	(61	) —	—	(61 )
Fixed asset write-offs and other	3,909	131	—	4,040	1,655	258	—	1,913
Recorded in Selling and General Administrative								
Other	78	—	—	78	—	—	—	—
Recorded in Rationalizations								
Severance and related costs	418	(28	) —	390	97	146	—	243

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Contract terminations	528	—	—	528	25	—	—	25
Total	\$26,452	\$1,415	\$—	\$27,867	\$2,148	\$404	\$—	\$2,552

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PART I (CONT'D)  
 GRAFTECH INTERNATIONAL LTD. AND SUBSIDIARIES  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
 (Unaudited)

The following table represents the roll-forward of the liability incurred for employee termination benefits and contract termination costs incurred in connection with the the rationalization initiatives described above. This liability is recorded as a current liability on the Consolidated Balance Sheets.

2013 Plans

	(Dollars in thousands)	
Balance as of December 31, 2013	\$ 18,421	
Charges incurred	613	
Change in estimates	153	
Payments and settlements	(16,494)	)
Effect of change in currency exchange rates	(1,658)	)
Balance as of December 31, 2014	1,035	
Charges incurred	41	
Change in estimates	229	
Payments and settlements	(1,132)	)
Effect of change in currency exchange rates	(91)	)
Balance as of June 30, 2015	\$ 82	

2014 Engineered Solutions Rationalization

On July 29, 2014, we announced additional rationalization initiatives to increase profitability, reduce cost and improve global competitiveness in our Engineered Solutions segment. During the second quarter of 2014, worldwide pricing of our isomolded graphite products ("isomolded") within our Advanced Graphite Material ("AGM") product group, as well as our expectation of future pricing, significantly eroded, driven by significant over-capacity and recent competitor responses. In addition, solar product demand continued to erode, with polysilicon, silicon and silicon wafer production migrating to China. New competitors servicing this industry commenced production in China at pricing levels making the market now unprofitable. As a result of these conditions, the Company decided to cease isomolded production and pursue alternative supply chain relationships in our isomolded product line.

As a result of the above, we tested our long-lived assets used to produce advanced graphite materials for recovery, based on undiscounted cash flows from the use and eventual disposition of these assets. The carrying value of the assets exceeded these undiscounted cash flow and, accordingly, we estimated the fair-value of these long-lived assets based on a market participant view. This resulted in an impairment charge totaling 121.6 million during 2014, and included the impairment of certain acquired customer relationship and technology intangible assets.

Charges incurred related to the 2014 Engineered Solutions rationalization initiatives in 2015 are as follows:

2014	For the Three Months Ended June 30, 2014	For the Three Months Ended June 30, 2015
Engineered Solutions Rationalization	Engineered Solutions Segment (Dollars in thousands)	
Recorded in Cost of Sales		
Inventory loss	10,562	109
Fixed asset write-offs and other	—	360

Recorded in Rationalizations

Severance and related costs	—	(733	)
Total	\$ 10,562	\$(264	)

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## PART I (CONT'D)

## GRAFTECH INTERNATIONAL LTD. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

2014	For the Six Months Ended June 30,	For the Six Months Ended June 30,
Engineered Solutions Rationalization	2014	2015
	Engineered Solutions Segment (Dollars in thousands)	
Recorded in Cost of Sales		
Inventory loss	\$ 10,562	\$ 543
Fixed asset write-offs and other	—	358
Recorded in Rationalizations		
Severance and related costs	—	(749 )
Contract terminations	—	50
Total	\$ 10,562	\$ 202

The following table represents the roll-forward of the liability incurred for employee termination benefits and contract termination costs incurred in connection with the 2014 Engineered Solutions rationalization initiatives described above. This liability is recorded as a current liability on the Consolidated Balance Sheets.

## 2014 Engineered Solutions Plan

	(Dollars in thousands)
Balance as of December 31, 2013	\$ —
Charges incurred	2,611
Change in estimates	(40 )
Payments and settlements	(916 )
Balance as of December 31, 2014	1,655
Charges incurred	50
Change in estimates	(749 )
Payments and settlements	(780 )
Balance as of June 30, 2015	\$ 176

## 2014 Corporate and Research &amp; Development Rationalization

During the third quarter of 2014, we announced the conclusion of another phase of our on-going company-wide cost savings assessment. This resulted in changes to the Company's operating and management structure in order to streamline, simplify and decentralize the organization. These actions are designed to reduce costs by a combination of reduced contractor costs, attrition, early retirements and layoffs. Additionally, the Company downsized its corporate functions by approximately 25 percent, relocated to a smaller, more cost effective corporate headquarters and established a new Technology and Innovation Center. The 2014 Corporate and Research and Development rationalization plan will result in approximately \$20 million of charges consisting of severance, accelerated depreciation and other related costs, of which approximately \$14 million have been incurred through June 30, 2015. Approximately \$12 million of these costs will be cash outlays, the majority of which are expected to be disbursed in 2015.



## PART I (CONT'D)

## GRAFTECH INTERNATIONAL LTD. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Charges incurred related to the 2014 Corporate and Research & Development rationalization initiatives for 2015 are as follows:

2014 Corporate,

Research and  
Development

Rationalization

For the Three Months Ended June 30, 2015

For the Six Months Ended June 30, 2015

Industrial Materials Segment	Engineered Solutions Segment	Corp, R&D and Other	Total
------------------------------------	------------------------------------	---------------------------	-------

Industrial Materials Segment	Engineered Solutions Segment	Corp, R&D and Other	Total
------------------------------------	------------------------------------	---------------------------	-------

(Dollars in thousands)

Recorded in Cost of Sales

Fixed asset

write-offs

and other

Recorded in Research and Development

Accelerated

depreciation

Recorded in Selling and General Administrative

Other

Recorded in Rationalizations

Severance

and related

costs

Total

The following table represents the roll-forward of the liability incurred for employee termination benefits and contract termination costs incurred in connection with the 2014 Corporate and Research & Development rationalization initiatives described above. This liability is recorded as a current liability on the Consolidated Balance Sheets.

2014 Corporate and R&amp;D Plan

	(Dollars in thousands)
Balance as of December 31, 2013	\$ —
Charges incurred	8,159
Change in estimates	21
Payments and settlements	(1,155 )
Effect of change in currency exchange rates	(152 )
Balance as of December 31, 2014	6,873
Charges incurred	(34 )
Change in estimates	(28 )
Payments and settlements	(4,199 )
Effect of change in currency exchange rates	(5 )
Balance as of June 30, 2015	\$ 2,607

2015 Advanced Graphite Materials Rationalization



On March 2, 2015, GrafTech announced plans to further optimize the production platform for its advanced graphite materials business. These actions included the closure of our Notre Dame, France facility and further reductions in force in our Columbia, Tennessee facility and other locations totaling approximately 85 people. The 2015 Advanced Graphite Materials rationalization plan

## PART I (CONT'D)

## GRAFTECH INTERNATIONAL LTD. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

will result in approximately \$10 million of charges consisting of severance, inventory losses and other related costs. Approximately \$8 million of these costs will be cash outlays, the majority of which are expected to be disbursed in 2015.

Charges incurred related to the 2015 Advanced Graphite Materials rationalization initiative for the three and six months ended June 30, 2015 are as follows:

2015 Advanced Graphite Materials Rationalization	For the Three Months Ended June 30, 2015 Engineered Solutions Segment	For the Six Months Ended June 30, 2015
Recorded in Cost of Sales		
Inventory loss	35	404
Fixed asset write-offs and other	461	356
Recorded in Selling and General Administrative		
Other	292	295
Recorded in Rationalizations		
Severance and related costs	2,220	4,601
Contract terminations	154	154
Total	\$3,162	\$5,810

The following table represents the roll-forward of the liability incurred for employee termination benefits and contract termination costs incurred in connection with the 2015 Advanced Graphite Materials rationalization initiative described above. This liability is recorded as a current liability on the Consolidated Balance Sheets.

## 2015 Advanced Graphite Materials Rationalization

	(Dollars in thousands)
Balance as of December 31, 2014	\$ —
Charges incurred	4,834
Payments and settlements	(263 )
Effect of change in currency exchange rates	(38 )
Balance as of June 30, 2015	\$4,533

## (4) Stock-Based Compensation

For the three months ended June 30, 2014 and 2015, we recognized stock-based compensation expense of \$2.2 million and \$1.1 million, respectively. Substantially all of the expense, \$1.6 million and \$1.0 million, respectively, was recorded as selling and administrative expenses in the Consolidated Statements of Operations, with the remaining expenses recorded as cost of sales and research and development.

For the six months ended June 30, 2014 and 2015, we recognized stock-based compensation expense of \$2.8 million and \$2.7 million, respectively. Substantially all of the expense, \$2.1 million and \$2.5 million, respectively, was recorded as selling and administrative expenses in the Consolidated Statements of Operations, with the remaining expenses recorded as cost of sales and research and development.

As of June 30, 2015, the total compensation cost related to non-vested restricted stock, performance shares based on current forecasts, and stock options not yet recognized was \$8.4 million, which will be recognized over the remaining weighted average life of 1.68 years.

## PART I (CONT'D)

## GRAFTECH INTERNATIONAL LTD. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

## Restricted Stock and Performance Shares

Restricted stock and performance share awards activity under the plans for the six months ended June 30, 2015 was:

	Number of Shares	Weighted- Average Grant Date Fair Value
Outstanding unvested as of January 1, 2015	1,814,130	\$6.31
Granted	19,969	8.31
Vested	(55,211)	) 10.23
Forfeited/canceled/expired	(188,407)	) 6.42
Outstanding unvested as of June 30, 2015	1,590,481	6.18

## Stock Options

Stock option activity under the plans for the six months ended June 30, 2015 was:

	Number of Shares	Weighted- Average Exercise Price
Outstanding as of January 1, 2015	2,042,074	\$10.93
Forfeited/canceled/expired	(203,592)	) 10.77
Outstanding as of June 30, 2015	1,838,482	10.95

## (5) Earnings per Share

The following table shows the information used in the calculation of our share counts for basic and diluted earnings per share:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2014	2015	2014	2015
Weighted average common shares outstanding for basic calculation	135,963,054	137,252,356	135,713,004	137,112,630
Add: Effect of stock options and restricted stock	—	—	—	—
Weighted average common shares outstanding for diluted calculation	135,963,054	137,252,356	135,713,004	137,112,630

Basic earnings per common share are calculated by dividing net income (loss) by the weighted average number of common shares outstanding. Diluted earnings per share are calculated by dividing net income (loss) by the sum of the weighted average number of common shares outstanding plus the additional common shares that would have been outstanding if potentially dilutive securities had been issued.

The weighted average common shares outstanding for the diluted calculation excludes consideration of stock options covering 1,079,251 shares in both the three and six months ended June 30, 2014, as these shares are anti-dilutive. The weighted average common shares outstanding for the diluted calculation excludes consideration of stock options covering 1,359,199 shares in both the three and six months ended June 30, 2015, as these shares are anti-dilutive.

PART I (CONT'D)  
 GRAFTECH INTERNATIONAL LTD. AND SUBSIDIARIES  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
 (Unaudited)

(6) Segment Reporting

We operate in two reportable segments: Industrial Materials and Engineered Solutions.

**Industrial Materials.** Our Industrial Materials segment manufactures and delivers high quality graphite electrodes, refractory products and needle coke products. Electrodes are key components of the conductive power systems used to produce steel and other non-ferrous metals. Refractory products are used in blast furnaces and submerged arc furnaces due to their high thermal conductivity and the ease with which they can be machined to large or complex shapes. Needle coke, a crystalline form of carbon derived from decant oil, is the key ingredient in, and is used primarily in, the production of graphite electrodes.

**Engineered Solutions.** The Engineered Solutions segment includes advanced electronics technologies, advanced graphite materials, advanced composite materials and advanced materials. Advanced electronics technologies products consist of electronic thermal management solutions, fuel cell components and sealing materials. Advanced graphite materials are highly engineered synthetic graphite products used in many areas due to their unique properties and the ability to tailor them to specific solutions. These products are used in transportation, alternative energy, metallurgical, chemical, oil and gas exploration and various other industries. Advanced composite materials are highly engineered carbon products that are woven into various shapes primarily to support the aerospace and defense industries. Advanced materials use carbon and graphite powders as components or additives in a variety of industries, including metallurgical processing, battery and fuel cell components, and polymer additives.

We continue to evaluate the performance of our segments based on segment operating income. Intersegment sales and transfers are not material and the accounting policies of the reportable segments are the same as those for our Consolidated Financial Statements as a whole. Prior to 2014, certain global expenses such as research and development, shared IT and accounting services as well as corporate headquarter's finance, HR, legal and executive management were allocated to the segments mostly based on each segment's contribution to consolidated sales. During 2014, as part of our initiative to decentralize the organization and reduce the costs of the global headquarter functions, the performance measure of our existing segments was changed to reflect our new management and operating structure. We currently exclude such expenses from the segment operating income measure and report them under "Corporate, R&D and Other Expenses" in order to reconcile to the consolidated operating income of the Company. The following tables summarize financial information concerning our reportable segments and all prior periods have been recast to reflect our new methodology:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2014	2015	2014	2015
	(Dollars in thousands)		(Dollars in thousands)	
Net sales to external customers:				
Industrial Materials	\$206,655	\$125,012	\$425,431	\$290,049
Engineered Solutions	77,529	40,110	139,544	82,284
Total net sales	\$284,184	\$165,122	\$564,975	\$372,333
Operating (loss) income:				
Industrial Materials	\$1,060	\$3,094	\$2,660	\$(22,804)
Engineered Solutions	(124,664)	(3,455)	(119,259)	(7,848)
Corporate, R&D and Other expenses	(15,884)	(12,636)	(29,958)	(28,178)
Total operating loss	\$(139,488)	\$(12,997)	\$(146,557)	\$(58,830)

Reconciliation of segment operating loss to  
 loss before provision for income taxes

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Other expense (income), net	\$(41	) \$699	\$753	\$1,092
Interest expense	9,155	9,195	18,154	18,116
Interest income				