

ENCORE WIRE CORP  
Form 10-Q  
August 07, 2012  
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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, 2012

For the quarterly period ended

June 30, 2012

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: 000-20278

# ENCORE WIRE CORPORATION

(Exact name of registrant as specified in its charter)

|                                                                                                     |                                                              |
|-----------------------------------------------------------------------------------------------------|--------------------------------------------------------------|
| <b>Delaware</b><br>(State or other jurisdiction of<br>incorporation or organization)                | <b>75-2274963</b><br>(I.R.S. Employer<br>Identification No.) |
| <b>1329 Millwood Road</b><br><br><b>McKinney, Texas</b><br>(Address of principal executive offices) | <b>75069</b><br>(Zip Code)                                   |
| <b>Registrant's telephone number, including area code: (972) 562-9473</b>                           |                                                              |

N/A

(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 ☐

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 <input type="checkbox"/>                                             | Accelerated filer <input checked="" type="checkbox"/> |
| Non-accelerated filer <input type="checkbox"/> (Do not check if a smaller reporting company) | Smaller reporting company <input type="checkbox"/>    |

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

Number of shares of Common Stock, par value \$0.01, outstanding as of Aug 6, 2012: 20,656,352

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**ENCORE WIRE CORPORATION**

**FORM 10-Q**

**FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2012**

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## ENCORE WIRE CORPORATION

## CONSOLIDATED BALANCE SHEETS

| In Thousands of Dollars                                      | June 30,<br>2012<br>(Unaudited) | December 31,<br>2011<br>(See Note) |
|--------------------------------------------------------------|---------------------------------|------------------------------------|
| <b>ASSETS</b>                                                |                                 |                                    |
| Current assets:                                              |                                 |                                    |
| Cash and cash equivalents                                    | \$ 47,727                       | \$ 112,298                         |
| Accounts receivable, net of allowance of \$2,100 and \$2,102 | 205,535                         | 199,366                            |
| Inventories                                                  | 52,505                          | 63,491                             |
| Income taxes receivable                                      | 1,015                           |                                    |
| Deferred income taxes                                        | 2,633                           |                                    |
| Prepaid expenses and other                                   | 1,135                           | 1,899                              |
| <b>Total current assets</b>                                  | <b>310,550</b>                  | <b>377,054</b>                     |
| Property, plant and equipment at cost:                       |                                 |                                    |
| Land and land improvements                                   | 18,124                          | 17,971                             |
| Construction-in-progress                                     | 29,897                          | 12,480                             |
| Buildings and improvements                                   | 76,055                          | 75,952                             |
| Machinery and equipment                                      | 191,725                         | 186,032                            |
| Furniture and fixtures                                       | 8,193                           | 7,947                              |
| <b>Total property, plant and equipment</b>                   | <b>323,994</b>                  | <b>300,382</b>                     |
| Accumulated depreciation                                     | (168,271)                       | (161,550)                          |
| <b>Property, plant and equipment net</b>                     | <b>155,723</b>                  | <b>138,832</b>                     |
| Other assets                                                 | 626                             | 260                                |
| <b>Total assets</b>                                          | <b>\$ 466,899</b>               | <b>\$ 516,146</b>                  |

Note: The consolidated balance sheet at December 31, 2011, as presented, is derived from the audited consolidated financial statements at that date.

See accompanying notes.

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## ENCORE WIRE CORPORATION

## CONSOLIDATED BALANCE SHEETS (continued)

|                                                                       | June 30,<br>2012<br>(Unaudited) | December 31,<br>2011<br>(See Note) |
|-----------------------------------------------------------------------|---------------------------------|------------------------------------|
| In Thousands of Dollars, Except Share Data                            |                                 |                                    |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>                           |                                 |                                    |
| Current liabilities:                                                  |                                 |                                    |
| Trade accounts payable                                                | \$ 31,571                       | \$ 14,676                          |
| Accrued liabilities                                                   | 18,559                          | 25,312                             |
| Income taxes payable                                                  |                                 | 1,174                              |
| Deferred income taxes                                                 |                                 | 1,408                              |
| <b>Total current liabilities</b>                                      | <b>50,130</b>                   | <b>42,570</b>                      |
| Non-current deferred income taxes                                     | 16,964                          | 15,833                             |
| <b>Commitments and contingencies</b>                                  |                                 |                                    |
| Stockholders' equity:                                                 |                                 |                                    |
| Preferred stock, \$.01 par value:                                     |                                 |                                    |
| Authorized shares 2,000,000; none issued                              |                                 |                                    |
| Common stock, \$.01 par value:                                        |                                 |                                    |
| Authorized shares 40,000,000; Issued shares 26,590,203 and 26,586,703 | 266                             | 266                                |
| Additional paid-in capital                                            | 47,861                          | 47,342                             |
| Treasury stock, at cost 5,934,651 and 3,160,401 shares                | (88,134)                        | (21,496)                           |
| Retained earnings                                                     | 439,812                         | 431,631                            |
| <b>Total stockholders' equity</b>                                     | <b>399,805</b>                  | <b>457,743</b>                     |
| <b>Total liabilities and stockholders' equity</b>                     | <b>\$ 466,899</b>               | <b>\$ 516,146</b>                  |

Note: The consolidated balance sheet at December 31, 2011, as presented, is derived from the audited consolidated financial statements at that date.

See accompanying notes.

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### ENCORE WIRE CORPORATION CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

| In Thousands, Except Per Share Data                          | Quarter Ended<br>June 30, |            | Six Months Ended<br>June 30, |            |
|--------------------------------------------------------------|---------------------------|------------|------------------------------|------------|
|                                                              | 2012                      | 2011       | 2012                         | 2011       |
| Net sales                                                    | \$ 264,730                | \$ 309,469 | \$ 545,196                   | \$ 612,820 |
| Cost of goods sold                                           | 245,339                   | 278,837    | 501,344                      | 548,432    |
| Gross profit                                                 | 19,391                    | 30,632     | 43,852                       | 64,388     |
| Selling, general, and administrative expenses                | 15,327                    | 16,083     | 30,404                       | 34,232     |
| Operating income                                             | 4,064                     | 14,549     | 13,448                       | 30,156     |
| Net interest and other (income) expenses                     | (8)                       |            | (28)                         | (5)        |
| Income before income taxes                                   | 4,072                     | 14,549     | 13,476                       | 30,161     |
| Provision for income taxes                                   | 1,702                     | 5,088      | 4,413                        | 10,046     |
| Net income                                                   | \$ 2,370                  | \$ 9,461   | \$ 9,063                     | \$ 20,115  |
| Net income per common and common equivalent share basic      | \$ 0.11                   | \$ 0.41    | \$ 0.40                      | \$ 0.87    |
| Weighted average common and common equivalent shares basic   | 21,997                    | 23,264     | 22,712                       | 23,241     |
| Net income per common and common equivalent share diluted    | \$ 0.11                   | \$ 0.40    | \$ 0.40                      | \$ 0.86    |
| Weighted average common and common equivalent shares diluted | 22,037                    | 23,405     | 22,757                       | 23,392     |
| Cash dividends declared per share                            | \$ 0.02                   | \$ 0.02    | \$ 0.04                      | \$ 0.04    |

See accompanying notes.

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ENCORE WIRE CORPORATION  
CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

|                                                                                             | Six Months Ended |                 |
|---------------------------------------------------------------------------------------------|------------------|-----------------|
|                                                                                             | June 30,         |                 |
| In Thousands of Dollars                                                                     | 2012             | 2011            |
| <b>OPERATING ACTIVITIES</b>                                                                 |                  |                 |
| Net income                                                                                  | \$ 9,063         | \$ 20,115       |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: |                  |                 |
| Depreciation and amortization                                                               | 7,236            | 6,867           |
| Deferred income taxes                                                                       | (2,910)          | 4               |
| Other                                                                                       | 372              | (305)           |
| Changes in operating assets and liabilities:                                                |                  |                 |
| Accounts receivable                                                                         | (6,168)          | (56,386)        |
| Inventories                                                                                 | 10,986           | (13,051)        |
| Trade accounts payable and accrued liabilities                                              | 10,197           | (4,050)         |
| Other assets and liabilities                                                                | 380              | (773)           |
| Current income taxes receivable / payable                                                   | (2,183)          | (3,040)         |
| <b>NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES</b>                                  | <b>26,973</b>    | <b>(50,619)</b> |
| <b>INVESTING ACTIVITIES</b>                                                                 |                  |                 |
| Purchases of property, plant and equipment                                                  | (24,042)         | (5,515)         |
| Proceeds from sale of assets                                                                | 11               |                 |
| <b>NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES</b>                                  | <b>(24,031)</b>  | <b>(5,515)</b>  |
| <b>FINANCING ACTIVITIES</b>                                                                 |                  |                 |
| Proceeds from issuances of common stock                                                     | 56               | 613             |
| Purchase of treasury stock                                                                  | (66,638)         |                 |
| Dividends paid                                                                              | (937)            | (929)           |
| Excess tax benefits of options exercised                                                    | 6                |                 |
| <b>NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES</b>                                  | <b>(67,513)</b>  | <b>(316)</b>    |
| Net increase (decrease) in cash and cash equivalents                                        | (64,571)         | (56,450)        |
| Cash and cash equivalents at beginning of period                                            | 112,298          | 103,252         |
| Cash and cash equivalents at end of period                                                  | \$ 47,727        | \$ 46,802       |

See accompanying notes.

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## ENCORE WIRE CORPORATION

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

June 30, 2012

## NOTE 1 BASIS OF PRESENTATION

The unaudited consolidated financial statements of Encore Wire Corporation (the Company) have been prepared in accordance with U.S. generally accepted accounting principles for interim information and the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete annual financial statements. In the opinion of management, all adjustments, consisting only of normal recurring adjustments considered necessary for a fair presentation, have been included. Results of operations for interim periods presented do not necessarily indicate the results that may be expected for the entire year. These financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2011.

## NOTE 2 INVENTORIES

Inventories are stated at the lower of cost, determined by the last-in, first-out (LIFO) method, or market.

Inventories consist of the following:

| In Thousands of Dollars            | June 30,<br>2012 | December 31,<br>2011 |
|------------------------------------|------------------|----------------------|
| Raw materials                      | \$ 16,551        | \$ 18,482            |
| Work-in-process                    | 26,296           | 22,955               |
| Finished goods                     | 82,012           | 84,819               |
| Total                              | 124,859          | 126,256              |
| Adjust to LIFO cost                | (72,354)         | (62,765)             |
| Lower of cost or market adjustment | 0                |                      |
| Inventory, net                     | \$ 52,505        | \$ 63,491            |

LIFO pools are established at the end of each fiscal year. During the first three quarters of every year, LIFO calculations are based on the inventory levels and costs at that time. Accordingly, interim LIFO balances will fluctuate up and down in tandem with inventory levels and costs.

During the first six months of 2011 the Company did not liquidate any LIFO inventory layers established in prior years. During the first six months of 2012, the Company liquidated a portion of the layer established in 2011. As a result, under the LIFO method, this inventory layer was liquidated at historical costs that were higher than current costs, which negatively impacted net income for the second quarter and the first six months of 2012 by \$383,000. In the fourth quarter of 2011, as part of the Company's

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aforementioned expansion into aluminum wire products and in anticipation of the start of production at the Company's new aluminum wire plant in 2012, the Company began a new aluminum wire inventory pool which is accounted for separately from the Company's copper wire inventory pool. The Company established this new aluminum wire pool in accordance with U.S. GAAP, which requires that new inventory items not previously present in significant quantities and having qualities significantly different from those items previously inventoried, as is the case with the physical, chemical, and cost differences between copper and aluminum metals, be accounted for separately.

### **NOTE 3 ACCRUED LIABILITIES**

Accrued liabilities consist of the following:

| In Thousands of Dollars        | June 30,<br>2012 | December 31,<br>2011 |
|--------------------------------|------------------|----------------------|
| Sales volume discounts payable | \$ 11,649        | \$ 16,220            |
| Property taxes payable         | 1,447            | 2,809                |
| Commissions payable            | 2,152            | 2,053                |
| Accrued salaries               | 2,172            | 3,548                |
| Other accrued liabilities      | 1,139            | 682                  |
| Total accrued liabilities      | \$ 18,559        | \$ 25,312            |

### **NOTE 4 INCOME TAXES**

Income taxes were accrued at an effective rate of 41.8% in the second quarter of 2012 versus 35.0% in the second quarter of 2011, consistent with the Company's estimated liabilities. The increase in the effective rate was due to a moderate change in the proportional effects of permanent items on the effective rate. For the six months ended June 30, the Company's effective tax rate was approximately 32.7% in 2012 and 33.3% in 2011. The year to date rate in 2012 is comparable to 2011.

### **NOTE 5 EARNINGS PER SHARE**

Net earnings (loss) per common and common equivalent share are computed using the weighted average number of shares of common stock and common stock equivalents outstanding during each period. If dilutive, the effect of stock options, treated as common stock equivalents, is calculated using the treasury stock method.

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The following table sets forth the computation of basic and diluted net earnings (loss) per share:

| In Thousands                                                                 | Quarters Ended   |                  |
|------------------------------------------------------------------------------|------------------|------------------|
|                                                                              | June 30,<br>2012 | June 30,<br>2011 |
| <b>Numerator:</b>                                                            |                  |                  |
| Net income (loss)                                                            | \$ 2,370         | \$ 9,461         |
| <b>Denominator:</b>                                                          |                  |                  |
| Denominator for basic earnings per share    weighted average shares          | 21,997           | 23,264           |
| <b>Effect of dilutive securities:</b>                                        |                  |                  |
| Employee stock options                                                       | 40               | 141              |
| <b>Denominator for diluted earnings per share    weighted average shares</b> | <b>22,037</b>    | <b>23,405</b>    |

The number of weighted average employee stock options excluded from the determination of diluted earnings per share for the second quarter was 192,500 in 2012 and 80,500 in 2011. Such options were anti-dilutive for the respective periods.

The following table sets forth the computation of basic and diluted net earnings (loss) per share:

| In Thousands                                                                 | Six Months Ended |                  |
|------------------------------------------------------------------------------|------------------|------------------|
|                                                                              | June 30,<br>2012 | June 30,<br>2011 |
| <b>Numerator:</b>                                                            |                  |                  |
| Net income (loss)                                                            | \$ 9,063         | \$ 20,115        |
| <b>Denominator:</b>                                                          |                  |                  |
| Denominator for basic earnings per share    weighted average shares          | 22,712           | 23,241           |
| <b>Effect of dilutive securities:</b>                                        |                  |                  |
| Employee stock options                                                       | 45               | 151              |
| <b>Denominator for diluted earnings per share    weighted average shares</b> | <b>22,757</b>    | <b>23,392</b>    |

The number of weighted average employee stock options excluded from the determination of diluted earnings per share for the six months ended June 30 was 165,879 in 2012 and 80,500 in 2011. Such options were anti-dilutive for the respective periods.

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### **NOTE 6 DEBT**

The Company is party to a Financing Agreement with two banks, Bank of America, N.A., as Agent, and Wells Fargo Bank, National Association (as amended, the "Financing Agreement"). The Financing Agreement extends through August 6, 2013, and provides for maximum borrowings of the lesser of \$150,000,000 or the amount of eligible accounts receivable plus the amount of eligible finished goods and raw materials, less any reserves established by the banks. The calculated maximum borrowing amount available at June 30, 2012, as computed under the Financing Agreement, was \$149,660,000. Borrowings under the line of credit bear interest, at the Company's option, at either (1) LIBOR plus a margin that varies from 1.0% to 1.75% depending upon the ratio of debt outstanding to adjusted earnings or (2) the base rate (which is the higher of the federal funds rate plus 0.5% or the prime rate) plus 0% to 0.25% (depending upon the ratio of debt outstanding to adjusted earnings). A commitment fee ranging from 0.20% to 0.375% (depending upon the ratio of debt outstanding to adjusted earnings) is payable on the unused line of credit. At June 30, 2012, there were no borrowings outstanding under the Financing Agreement. Obligations under the Financing Agreement are the only contractual borrowing obligations or commercial borrowing commitments of the Company.

Obligations under the Financing Agreement are unsecured and contain customary covenants and events of default. The Company was in compliance with the covenants as of June 30, 2012.

### **NOTE 7 STOCKHOLDERS' EQUITY**

On November 10, 2006, the Board of Directors approved a stock repurchase program authorizing the Company to repurchase up to 1,000,000 shares of its common stock through December 31, 2007 on the open market or through privately negotiated transactions at prices determined by the President of the Company. The Company's Board of Directors has subsequently authorized annual extensions of this stock repurchase program. On May 11, 2012, the Board of Directors authorized the repurchase of up to 4 million shares of its common stock through March 31, 2013 under the previously approved stock repurchase program of the Company. On May 14, 2012, the Company repurchased 2,774,250 shares of common stock owned by Capital Southwest Venture Corporation at an aggregate purchase price of \$66,637,485, based on a price of \$24.02 per share. Appropriate consents to the repurchase were also obtained from lenders under the Company's Financing Agreement. The repurchase authorization now has 1,225,750 shares remaining. The repurchase represented approximately 11.8% of the outstanding shares of the Company as of the purchase date and was the only repurchase in the first six months of 2012. The Company did not repurchase any shares in the first six months of 2011. Other than net income and the stock repurchase, there were no material changes in stockholders' equity during the quarter and six months ended June 30, 2012.

### **NOTE 8 CONTINGENCIES**

On July 7, 2009, Southwire Company, a Delaware corporation ("Southwire"), filed a complaint for patent infringement against the Company and Cerro Wire, Inc. ("Cerro") in the United States District Court for the Eastern District of Texas. In the complaint, Southwire alleged that the Company infringed one or more claims of United States

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Patent No. 7,557,301 (the '301 patent'), entitled Method of Manufacturing Electrical Cable Having Reduced Required Force for Installation, by making and selling electrical cables, including the Company's Super Slick cables. The case has been transferred to the Northern District of Georgia and the parties have agreed to stay it pending reexamination of the '301 patent by the United States Patent and Trademark Office (the USPTO). On June 23, 2011, the USPTO issued an office action in the reexamination finally rejecting all the claims of the '301 patent. Southwire responded to these final rejections on August 8, 2011 by submitting substantially amended claims. The examiner determined that the amended claims captured patentable subject matter and on September 21, 2011 issued a notice that a reexamination certificate would issue evidencing the patentability of the amended claims. The reexamination certificate was issued on the '301 patent on December 27, 2011.

Although the parties convened on March 21, 2012 for a settlement conference regarding the '301 patent lawsuit, such settlement conference did not result in any negotiation, agreement, decision or other development that the Company believed is material to such lawsuit. At this point, the parties are planning a second conference to further discuss the issues.

On July 2, 2010, the Company filed a complaint against Southwire in the Northern District of Georgia. The complaint alleged that Southwire was using a deceptively misdescriptive trademark on its SimPull products, and that Southwire had made false statements about the Company's Slick Wire products. Southwire's United States Patent No. 7,749,024 (the '024 patent') issued on July 6, 2010. The morning the patent issued, the Company amended its complaint to seek a declaratory judgment that the Company's Slick Wire products do not infringe the '024 patent. Later that same day, Southwire filed a separate complaint against the Company and Cerro Wire in the Eastern District of Texas alleging infringement of the '024 patent. The Company's complaint against Southwire was stayed by agreement on April 11, 2011. The case will remain stayed until the USPTO issues a certificate of reexamination of the '024 patent. The complaint filed by Southwire in the Eastern District of Texas has been voluntarily dismissed and Southwire will have the option to pursue its claims against the Company in the Northern District of Georgia, once the reexamination is completed. On October 8, 2010, the Company filed a request with the USPTO for an inter partes reexamination of the '024 patent. On November 9, 2010, the USPTO ordered the reexamination of the '024 patent. In ordering reexamination of Southwire's '024 patent, the USPTO determined that the Company's submission of prior art raised a substantial new question of patentability of the claims of the '024 patent. On December 3, 2010, the USPTO issued a non-final office action rejecting all of the claims of the '024 Patent. Southwire filed a response to the non-final office action on February 3, 2011, which included legal arguments and supporting technical declarations. The Company filed its comments to the Southwire response on March 3, 2011, including points and authorities, legal arguments, and supporting technical declarations. On July 9, 2012, the Examiner issued an Action Closing Prosecution finally rejecting patent claims 4-7 and 9-12 in the reexamination of the '024 patent. Southwire may file a response to the final rejections on or before September 9, 2012. If Southwire files to respond, the Company has thirty (30) days from the date of service of the response to file written comments on Southwire's position.

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Southwire's complaints sought unspecified damages and injunctive relief. At this time, all pending litigation between Encore and Southwire has been dismissed or stayed by agreement of the parties.

The potentially applicable factual and legal issues related to the above claims asserted against the Company have not been resolved. The Company disputes all of Southwire's claims and alleged damages and intends to vigorously defend the lawsuits and vigorously pursue its own claims against Southwire if and when the litigation resumes.

The Company is from time to time involved in litigation, certain other claims and arbitration matters arising in the ordinary course of its business. The Company accrues for a liability when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. Significant judgment is required in both the determination of the probability of a loss and the determination as to whether a loss is reasonably estimable. Any such accruals are reviewed at least quarterly and adjusted to reflect the effects of negotiations, settlements, rulings, advice of legal counsel and technical experts and other information and events pertaining to a particular matter. To the extent there is a reasonable possibility (within the meaning of ASC 450) that probable losses could exceed amounts already accrued, if any, and the additional loss or range of loss is able to be estimated, management discloses the additional loss or range of loss.

For matters where the Company has evaluated that a loss is not probable, but is reasonably possible, the Company will disclose an estimate of the possible loss or range of loss or make a statement that such an estimate cannot be made. In some instances, for reasonably possible losses, the Company cannot estimate the possible loss or range of loss. The nature and progression of litigation can make it difficult to predict the impact a particular lawsuit will have on the Company. There are many reasons that the Company cannot make these assessments, including, among others, one or more of the following: the early stages of a proceeding; damages sought that are unspecified, unsupportable, unexplained or uncertain; discovery is incomplete; the complexity of the facts that are in dispute; the difficulty of assessing novel claims; the parties not having engaged in any meaningful settlement discussions; the possibility that other parties may share in any ultimate liability; and/or the often slow pace of litigation.

At this time, given the status of the proceedings, the complexities of the facts in dispute and the multiple claims involved, the Company has not concluded that a probable loss exists with respect to the Southwire litigation. Accordingly, no accrual has been made. Additionally, given the aforementioned uncertainties, the Company is unable to estimate any possible loss or range of losses for disclosure purposes.

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

### **General**

Encore is a low-cost manufacturer of electrical building wire and cable. The Company is a significant supplier of building wire for interior electrical wiring in commercial and industrial buildings, homes, apartments, and manufactured housing.

The Company's operating results in any given time period are driven by several key factors, including the volume of product produced and shipped, the cost of copper and other raw materials, the competitive pricing environment in the wire industry and the resulting influence on gross margins and the efficiency with which the Company's plants operate during the period, among others. Price competition for electrical wire and cable is intense, and the Company sells its products in accordance with prevailing market

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prices. Copper, a commodity product, is the principal raw material used by the Company in manufacturing its products. Copper accounted for approximately 86.1%, 81.1% and 73.5% of the Company's cost of goods sold during fiscal 2011, 2010 and 2009, respectively. The price of copper fluctuates, depending on general economic conditions and in relation to supply and demand and other factors, which causes monthly variations in the cost of copper purchased by the Company. The Company cannot predict copper prices in the future or the effect of fluctuations in the cost of copper on the Company's future operating results. Wire prices can, and frequently do change on a daily basis. This competitive pricing market for wire does not always mirror changes in copper prices, making margins highly volatile. With the Company's expansion into aluminum conductors in some of its building wire products, aluminum will slowly grow its percentage share of the raw materials cost for the Company. The Company is building a plant to expand the production of aluminum building wire as announced in a December 2011 press release. Historically, the cost of aluminum is much less than copper and also less volatile. With the volatility of both raw material prices and wire prices in the Company's end market, hedging raw materials can be risky. Historically, the Company has not engaged in hedging strategies for raw material purchases.

The following discussion and analysis relates to factors that have affected the operating results of the Company for the quarterly and six month periods ended June 30, 2012 and 2011. Reference should also be made to the audited financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2011.

## **Results of Operations**

### **Quarter Ended June 30, 2012 Compared to Quarter Ended June 30, 2011**

Net sales for the second quarter of 2012 were \$264.7 million compared with net sales of \$309.5 million for the second quarter of 2011. This dollar decrease was primarily the result of a 13.2% decrease in the average price of wire sold and a 4.0% decrease in the unit volume of copper wire shipped. Unit volume is measured in pounds of copper contained in the wire shipped during the period. Fluctuations in sales prices are primarily a result of changing copper raw material prices and product price competition. The average cost per pound of raw copper purchased decreased 14.1% in the second quarter of 2012 compared to the second quarter of 2011, and was the principal driver of the decreased average sales price of wire. In the second quarter of 2012, aluminum wire constituted 3.5% of the Company's net sales dollars compared to 1.0% in the second quarter of 2011.

Cost of goods sold decreased to \$245.3 million, or 92.7% of net sales, in the second quarter of 2012, compared to \$278.8 million, or 90.1% of net sales, in the second quarter of 2011. Gross profit decreased to \$19.4 million, or 7.3% of net sales, in the second quarter of 2012 versus \$30.6 million, or 9.9% of net sales, in the second quarter of 2011. The decreased gross profit dollars and gross profit margin percentages were primarily the result of an increase in total materials cost including the LIFO adjustment from 83.7% of net sales in the second quarter of 2011 to 84.3% in the second quarter of 2012, along with an increase in manufacturing labor, depreciation and overhead from 6.3% to 8.3% of net sales in the second quarter of 2011 versus the second quarter of 2012. The overhead percentage increased both from increased spending on machinery

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repairs and some gearing up for the new aluminum plant, as well as the fact that many components of overhead are semi-fixed and were being divided over a lower sales dollar denominator. The aluminum building wire plant is targeted to commence production in the second half of 2012. Building wire prices and margins were impacted negatively by the competitive pricing in the building wire industry. Several times during the quarter, the industry announced a price increase in the face of a couple days of upward movement in copper prices, only to have copper drop just after the effective date of the increase and effectively negate the increase. This disrupted some customer buying patterns and enticed competitors to cut or hold prices, resulting in lower margins for the Company.

Inventories are stated at the lower of cost, using the last-in, first out (LIFO) method, or market. The Company maintains two inventory pools for LIFO purposes. As permitted by U.S. generally accepted accounting principles, the Company maintains its inventory costs and cost of goods sold on a first-in, first-out (FIFO) basis and makes a monthly adjustment to adjust total inventory and cost of goods sold from FIFO to LIFO. The Company applies the lower of cost or market (LCM) test by comparing the LIFO cost of its raw materials, work-in-process and finished goods inventories to estimated market values, which are based primarily upon the most recent quoted market price of copper, aluminum and finished wire prices as of the end of each reporting period. The Company performs a lower of cost or market calculation quarterly. As of June 30, 2012, no LCM adjustment was required. However, decreases in copper and other material prices could necessitate establishing an LCM reserve in future periods. Additionally, future reductions in the quantity of inventory on hand could cause copper or other raw materials that are carried in inventory at costs different from the cost of copper and other raw materials in the period in which the reduction occurs to be included in costs of goods sold for that period at the different price.

Primarily due to decreasing copper costs and a small decrease in copper inventory quantities on hand during the second quarter of 2012, a LIFO adjustment was recorded decreasing cost of sales by \$7.6 million during the quarter.

Selling expenses, consisting of commissions and freight, for the second quarter of 2012 were \$11.2 million, or 4.2% of net sales, compared to \$12.6 million, or 4.1% of net sales, in the second quarter of 2011. Commissions paid to independent manufacturers' representatives are paid as a relatively stable percentage of sales, and therefore, declined \$1.6 million in concert with the decreased sales dollars. Additionally, although units shipped declined slightly, freight costs increased by \$0.2 million, or 0.3% of net sales as a result of increased fuel prices, smaller customer order quantities and small shifts in demand from various areas of the country. General and administrative expenses were \$4.1 million, or 1.6% of net sales, in the second quarter of 2012 compared to \$3.5 million, or 1.1% of net sales, in the second quarter of 2011. The provision for bad debts was \$0 for the second quarters of 2012 and 2011.

Net interest and other (income) expense was virtually zero in the second quarters of 2012 and 2011. Income taxes were accrued at an effective rate of 41.8% in the second quarter of 2012, versus an effective rate of 35.0% in the second quarter of 2011. The increase in the effective rate was due to a moderate change in the proportional effects of permanent items on the effective rate.

As a result of the foregoing factors, the Company's net income decreased to \$2.4 million in the second quarter of 2012 from \$9.5 million in the second quarter of 2011.

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**Six Months Ended June 30, 2012 compared to Six Months Ended June 30, 2011**

Net sales for the first six months of 2012 were \$545.2 million compared with net sales of \$612.8 million for the first half of 2011. This dollar decrease was the result of an 11.3% decrease in the average price of wire sold and a 2.2% decrease in the unit volume of copper wire sold, measured in pounds of copper contained in the wire. The average cost per pound of raw copper purchased decreased 13.7% in the first six months of 2012 compared to the first six months of 2011. In comparing the first half of 2012 to the first half of 2011, the average sales price of wire that contained a pound of copper decreased more than the average price of copper purchased during the period. Margins contracted as the spread between the price of wire sold and the cost of raw copper purchased decreased by 2.7%, due primarily to deteriorating industry pricing discipline. Fluctuations in sales prices are primarily a result of changing copper raw material prices and product price competition.

Cost of goods sold decreased to \$501.3 million in the first six months of 2012, compared to \$548.4 million in the first six months of 2011. Gross profit decreased to \$43.9 million, or 8.0% of net sales, in the first six months of 2012 versus \$64.4 million, or 10.5% of net sales, in the first six months of 2011. The decreased gross profit dollars were primarily the result of the 11.0% decrease in net sales dollars and the decreased copper spreads in the first six months of 2012 versus the same period in 2011 as discussed above.

As a result of decreasing copper costs in the second quarter and a small decrease in the amount of inventory on hand during the first six months of 2012, a LIFO adjustment was recorded increasing cost of sales by \$9.6 million during the six month period. Based on the current copper prices, there is no LCM adjustment necessary. Future reductions in the price of copper could require the Company to record an LCM adjustment against the related inventory balance, which would result in a negative impact on net income.

Selling expenses for the first six months of 2012 decreased to \$22.2 million, or 4.1% of net sales, compared to \$24.3 million, or 4.0% of net sales, in the same period of 2011. Commissions paid to independent manufacturers' representatives are calculated as a percentage of sales, and therefore, dropped \$2.9 million in concert with the decreased sales dollars. Freight costs increased \$0.9 million to \$9.9 million or 1.8% of net sales versus \$9.1 million or 1.5% of net sales as a result of increased fuel prices, smaller customer order quantities and small shifts in demand from various areas of the country. Commissions were 2.2% and 2.5% of net sales in the first six months of 2012 and 2011, respectively. General and administrative expenses decreased to \$8.2 million, or 1.5% of net sales, in the first six months of 2012 compared to \$10.0 million, or 1.6% of net sales, in the same period of 2011. The general and administrative costs declined primarily due to decreased legal and administrative costs. The provision for bad debts was zero in the first six months of 2012 and 2011, respectively.

Net interest and other expense (income) was \$28,000 of income in the first six months of 2012 compared to \$5,000 of income in the first half of 2011. Income taxes were accrued at an effective rate of 32.7% in the first six months of 2012 versus 33.3% in the first six months of 2011 consistent with the Company's estimated liabilities.

As a result of the foregoing factors, the Company's net income decreased to \$9.1 million in the first half of 2012 from \$20.1 million in the first half of 2011

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### **Liquidity and Capital Resources**

The Company maintains a substantial inventory of finished products to satisfy customers' prompt delivery requirements. As is customary in the building wire industry, the Company provides payment terms to most of its customers that exceed terms that it receives from its suppliers. Copper suppliers generally give very short payment terms, (less than 15 days) while the Company and the building wire industry give customers much longer terms. As a result of this timing difference, building wire companies must have sufficient cash and access to capital resources to finance their working capital needs, thereby creating a barrier to entry for companies who do not have sufficient liquidity and capital resources. The two largest components of working capital, receivables and inventory, and to some extent, capital expenditures are the primary drivers of the Company's liquidity needs. Generally, this will cause the cash balance to rise and fall inversely to the receivables and inventory balances. The receivables and inventories will rise and fall in concert with several factors, most notably the price of copper and other raw materials and the level of unit sales. Receivables will go up at the end of quarters with strong dollar sales and down as those sales decline. Inventory balances will rise and fall with the raw material price fluctuations and the level of units on hand at the end of any given quarter. Capital expenditures have historically been necessary to expand and update the production capacity of the Company's manufacturing operations. The Company has historically satisfied its liquidity and capital expenditure needs with cash generated from operations, borrowings under its various debt arrangements and sales of its common stock. The Company historically uses its revolving credit facility to manage day to day operating cash needs as required by daily fluctuations in working capital, and has the facility in place should such a need arise in the future.

The Company is party to a Financing Agreement with two banks, Bank of America, N.A., as Agent, and Wells Fargo Bank, National Association (as amended, the "Financing Agreement"). The Financing Agreement extends through August 6, 2013, and provides for maximum borrowings of the lesser of \$150,000,000 or the amount of eligible accounts receivable plus the amount of eligible finished goods and raw materials, less any reserves established by the banks. The calculated maximum borrowing amount available at June 30, 2012, as computed under the Financing Agreement, was \$149,660,000. Borrowings under the line of credit bear interest, at the Company's option, at either (1) LIBOR plus a margin that varies from 1.0% to 1.75% depending upon the ratio of debt outstanding to adjusted earnings or (2) the base rate (which is the higher of the federal funds rate plus 0.5% or the prime rate) plus 0% to 0.25% (depending upon the ratio of debt outstanding to adjusted earnings). A commitment fee ranging from 0.20% to 0.375% (depending upon the ratio of debt outstanding to adjusted earnings) is payable on the unused line of credit. At June 30, 2012, there were no borrowings outstanding under the Financing Agreement. Obligations under the Financing Agreement are the only contractual borrowing obligations or commercial borrowing commitments of the Company.

Obligations under the Financing Agreement are unsecured and contain customary covenants and events of default. The Company was in compliance with the covenants as of June 30, 2012.

Cash provided in operating activities was \$27.0 million in the first six months of 2012 compared to a use of cash of \$50.6 million in the first six months of 2011. The following

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changes in components of cash flow were notable. The Company had net income of \$9.1 million in the first six months of 2012 versus net income of \$20.1 million in the first six months of 2011. Accounts receivable increased in the first six months of 2012 and 2011, although at much different amounts, resulting in a use of cash of \$6.2 million and \$56.4 million, respectively, driving a lower use of cash of \$50.2 million in 2012 versus 2011. Accounts receivable increased in the first six months of both years, primarily due to the timing of sales in the quarters. With an average of 60 to 75 days of sales outstanding, quarters in which sales are more back-end loaded will have higher accounts receivable balances outstanding at quarter-end. Inventory dollars decreased in 2012, which provided an \$11.0 million source of cash, while inventory increased in 2011, resulting in a \$13.1 million use of cash. This swing in inventory resulted in an overall increase in cash provided of \$24.0 million in the first six months of 2012 versus the first six months of 2011. Trade accounts payable and accrued liabilities resulted in a \$14.2 million increase in cash provided in the first six months of 2012 versus the first six months of 2011 due primarily to the decrease in accounts payable, attributable primarily to the timing of inventory receipts at quarter end. These changes in cash flow were the primary drivers of the \$77.6 million increase in cash provided in operations in the first six months of 2012 versus the first six months of 2011.

Cash used in investing activities increased to \$24.0 million in the first six months of 2012 from \$5.5 million in the first six months of 2011. The funds were used primarily for the construction of the new aluminum wire plant, including deposits on equipment for that plant in 2012 and equipment purchases in 2011. Cash used by financing activities was \$67.5 million in the first six months of 2012 versus \$0.3 million in 2011. In May of 2012, the Company repurchased 2,774,250 shares of its common stock from Capital Southwest Venture Corporation for \$66.6 million. In the first six months of 2012, the Company's revolving line of credit remained at \$0. The Company's cash balance was \$47.7 million at June 30, 2012, versus \$46.8 million at June 30, 2011.

During the remainder of 2012, the Company expects its capital expenditures will consist primarily of expenditures related to the new aluminum building wire plant, including purchases of new manufacturing equipment. The total capital expenditures for all of 2012 associated with these projects are currently estimated to be between \$38 million and \$42 million. The Company also expects its future working capital requirements may fluctuate as a result of changes in unit sales volumes and the price of copper and other raw materials. The Company believes that the current cash balance, cash flow from operations, and the financing available from its revolving credit facility will satisfy working capital and capital expenditure requirements during 2012.

## **Information Regarding Forward Looking Statements**

This quarterly report on Form 10-Q contains various forward-looking statements (within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended) and information that is based on management's belief as well as assumptions made by and information currently available to management. The words believes, estimates, anticipates, plans, seeks, expects, intends and similar expressions identify some of the forward-looking statements. Although the Company believes that the expectations reflected in such forward-looking statements are reasonable, it can give no assurance that such expectations will prove to have been correct. Such statements are subject to certain risks, uncertainties and assumptions. Should one or more of these risks or uncertainties

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materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those expected. Among the key factors that may have a direct bearing on the Company's operating results are fluctuations in the economy and in the level of activity in the building and construction industry, demand for the Company's products, the impact of price competition and fluctuations in the price of copper. For more information regarding forward looking statements see Information Regarding Forward Looking Statements in Part II, Item 7 of the Company's Annual Report on Form 10-K for the year ended December 31, 2011, which is hereby incorporated by reference.

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

There have been no material changes from the information provided in Item 7A, Quantitative and Qualitative Disclosures About Market Risk, of the Company's Annual Report on Form 10-K for the year ended December 31, 2011.

### **Item 4. Controls and Procedures.**

The Company maintains controls and procedures designed to ensure that information required to be disclosed by it in the reports it files with or submits to the Securities and Exchange Commission (the SEC) is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms and to ensure that information required to be disclosed by the Company in such reports is accumulated and communicated to the Company's management, including the Chief Executive and Chief Financial Officers, as appropriate to allow timely decisions regarding required disclosure. Based on an evaluation of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report conducted by the Company's management, with the participation of the Chief Executive and Chief Financial Officers, the Chief Executive and Chief Financial Officers concluded that the Company's disclosure controls and procedures were effective to ensure that information required to be disclosed by the Company in the reports it files with or submits to the SEC is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms and to ensure that information required to be disclosed by the Company in such reports is accumulated and communicated to the Company's management, including the Chief Executive and Chief Financial Officers, as appropriate to allow timely decisions regarding required disclosure.

There have been no changes in the Company's internal control over financial reporting or in other factors that have materially affected, or are reasonably likely to materially affect, internal control over financial reporting during the period covered by this report.

## **PART II OTHER INFORMATION**

### **Item 1. Legal Proceedings.**

For information on the Company's legal proceedings, see Note 8 to the Company's consolidated financial statements included in Item 1 to this report and incorporated herein by reference.

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### Item 1A. Risk Factors.

There have been no material changes to the Company's risk factors as disclosed in Item 1A, Risk Factors, in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2011.

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

#### Issuer Purchases of Equity Securities<sup>(1)</sup>

| Period        |                | (a)<br>Total number<br>of<br>shares purchased | (b)<br>Average price<br>paid<br>per share | (c)<br>Total number<br>of<br>shares purchased<br>as part of publicly<br>announced plans<br>or programs | (d)<br>Maximum number<br>of shares that<br>may yet be<br>purchased<br>under<br>the plans or<br>programs |
|---------------|----------------|-----------------------------------------------|-------------------------------------------|--------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------|
| April 1, 2012 | April 30, 2012 |                                               |                                           |                                                                                                        | 2,598,549                                                                                               |
| May 1, 2012   | May 31, 2012   | 2,774,250 <sup>(2)</sup>                      | \$ 24.02                                  | 2,774,250                                                                                              | 1,225,750 <sup>(2)</sup>                                                                                |
| June 1, 2012  | June 30, 2012  |                                               |                                           |                                                                                                        | 1,225,750                                                                                               |
| Total         |                | 2,774,250                                     | \$ 24.02                                  | 2,774,250                                                                                              | 1,225,750                                                                                               |

- (1) On November 10, 2006, the Board of Directors approved a stock repurchase program authorizing the Company to repurchase up to 1,000,000 shares of its common stock through December 31, 2007 on the open market or through privately negotiated transactions at prices determined by the President of the Company. The Company's Board of Directors has subsequently authorized annual extensions of this stock repurchase program through March 31, 2013.
- (2) On May 11, 2012, the Board of Directors authorized the repurchase of up to 4 million shares of its common stock through March 31, 2013 under the previously approved stock repurchase program of the Company. On May 14, 2012, the Company repurchased 2,774,250 shares of common stock owned by Capital Southwest Venture Corporation at an aggregate purchase price of \$66,637,485, based on a price of \$24.02 per share.

### Item 6. Exhibits.

The information required by this Item 6 is set forth in the Index to Exhibits accompanying this Form 10-Q and incorporated herein by reference.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

ENCORE WIRE CORPORATION  
(Registrant)

Dated: August 7, 2012

/s/ DANIEL L. JONES  
Daniel L. Jones, President and  
Chief Executive Officer

Dated: August 7, 2012

/s/ FRANK J. BILBAN  
Frank J. Bilban, Vice President Finance,  
Chief Financial Officer,  
  
Treasurer and Secretary

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INDEX TO EXHIBITS

| Exhibit |                                                                                                                                                                                                                                                                                                 |
|---------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Number  | Description                                                                                                                                                                                                                                                                                     |
| 3.1     | Certificate of Incorporation of Encore Wire Corporation and all amendments thereto (filed as Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2009, and incorporated herein by reference).                                                            |
| 3.2     | Third Amended and Restated Bylaws of Encore Wire Corporation, as amended through February 27, 2012 (filed as Exhibit 3.2 to the Company's Annual Report on Form 10-K for the year ended December 31, 2011, and incorporated herein by reference).                                               |
| 4.1     | Form of certificate for Common Stock (filed as Exhibit 1 to the Company's registration statement on Form 8-A, filed with the SEC on June 4, 1992, and incorporated herein by reference).                                                                                                        |
| 4.2     | Registration Rights Agreement dated February 29, 2012 among the Company, Capital Southwest Corporation and Capital Southwest Venture Corporation (filed as Exhibit 4.2 to the Company's Annual Report on Form 10-K for the year ended December 31, 2011, and incorporated herein by reference). |
| 10.1    | Share Repurchase Agreement dated May 14, 2012 by and among the Company, Capital Southwest Corporation and Capital Southwest Venture Corporation (filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the SEC on May 18, 2012, and incorporated herein by reference).   |
| 31.1    | Certification by Daniel L. Jones, President and Chief Executive Officer of the Company, dated August 7, 2012 and submitted pursuant to Rule 13a-14(a)/15d-14(a) and pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.                                                                  |
| 31.2    | Certification by Frank J. Bilban, Vice President Finance, Treasurer, Secretary and Chief Financial Officer of the Company, dated August 7, 2012 and submitted pursuant to Rule 13a-14(a)/15d-14(a) and pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.                               |
| 32.1    | Certification by Daniel L. Jones, President and Chief Executive Officer of the Company, dated August 7, 2012 as required by 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.                                                                       |
| 32.2    | Certification by Frank J. Bilban, Vice President Finance, Treasurer, Secretary and Chief Financial Officer, dated August 7, 2012 as required by 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.                                                   |
| 101.INS | XBRL Instance Document                                                                                                                                                                                                                                                                          |

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|         |                                                        |
|---------|--------------------------------------------------------|
| 101.SCH | XBRL Taxonomy Extension Schema Document                |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document  |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document        |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document   |