CARPENTER TECHNOLOGY CORP
Form 10-Q
October 26, 2017
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2017

or

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

For the transition period from to

Commission File Number 1-5828

CARPENTER TECHNOLOGY CORPORATION
(Exact name of Registrant as specified in its Charter)

Delaware	23-0458500
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1735 Market Street, 15th Floor Philadelphia, Pennsylvania	19103
(Address of principal executive offices)	(Zip Code)

610-208-2000
(Registrant’s telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files. Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer:	x	Accelerated filer:	o
Non-accelerated filer:	o (Do not check if a smaller reporting company)	Smaller reporting company:	o
		Emerging growth company	o

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. o

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

The number of shares outstanding of the issuer's common stock as of October 19, 2017 was 46,816,607.

Table of Contents

CARPENTER TECHNOLOGY CORPORATION
FORM 10-Q
INDEX

Table of Contents

PART I - FINANCIAL INFORMATION
Item 1. Financial Statements

CARPENTER TECHNOLOGY CORPORATION
CONSOLIDATED BALANCE SHEETS
(Unaudited)
(in millions, except share data)

	September 30, 2017	June 30, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$ 24.9	$66.3
Accounts receivable, net	294.6	290.4
Inventories	737.3	690.4
Other current assets	54.9	46.5
Total current assets	1,111.7	1,093.6
Property, plant and equipment, net	1,308.7	1,316.8
Goodwill	263.4	263.4
Other intangibles, net	63.2	64.9
Deferred income taxes	7.5	7.6
Other assets	138.0	131.8
Total assets	$ 2,892.5	$2,878.1
LIABILITIES		
Current liabilities:		
Credit agreement borrowings	$ 3.3	$—
Current portion of long-term debt	55.0	55.0
Accounts payable	212.5	201.1
Accrued liabilities	110.8	139.9
Total current liabilities	381.6	396.0
Long-term debt, net of current portion	549.8	550.0
Accrued pension liabilities	372.1	378.3
Accrued postretirement benefits	123.3	122.6
Deferred income taxes	191.4	184.8
Other liabilities	43.3	47.8
Total liabilities	1,661.5	1,679.5
Contingencies and commitments (see Note 8)		
STOCKHOLDERS’ EQUITY		
Common stock — authorized 100,000,000 shares; issued 55,395,245 shares at September 30, 2017 and 55,349,658 shares at June 30, 2017; outstanding 46,803,324 shares at September 30, 2017 and 46,753,180 shares at June 30, 2017	277.0	276.7
Capital in excess of par value	289.9	284.8
Reinvested earnings	1,336.6	1,321.8
Common stock in treasury (8,591,921 shares and 8,596,478 shares at September 30, 2017 and June 30, 2017, respectively), at cost	(341.4)	(341.6)
Accumulated other comprehensive loss	(331.1)	(343.1)
Total stockholders' equity	1,231.0	1,198.6
Total liabilities and stockholders' equity	$ 2,892.5	$2,878.1

See accompanying notes to consolidated financial statements.

Table of Contents

CARPENTER TECHNOLOGY CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(in millions, except per share data)

	Three Months Ended September 30,	
	2017	2016
Net sales	$479.8	$389.0
Cost of sales	394.2	343.0
Gross profit	85.6	46.0
Selling, general and administrative expenses	43.9	44.6
Operating income	41.7	1.4
Interest expense	(7.2)	(7.3)
Other income, net	0.7	0.6
Income (loss) before income taxes	35.2	(5.3)
Income tax expense	11.8	0.9
Net income (loss)	$23.4	$(6.2)
EARNINGS (LOSS) PER COMMON SHARE:		
Basic	$0.49	$(0.13)
Diluted	$0.49	$(0.13)
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING:		
Basic	47.1	46.9
Diluted	47.3	46.9
Cash dividends per common share	$0.18	$0.18

See accompanying notes to consolidated financial statements.

Table of Contents

CARPENTER TECHNOLOGY CORPORATION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)
($ in millions)

	Three Months Ended September 30, 2017		2016		
Net income (loss)	$	23.4	$	(6.2	)
Other comprehensive income, net of tax					
Pension and postretirement benefits, net of tax of $(1.3) and $(10.5), respectively	2.1		17.4		
Net gain on derivative instruments, net of tax of $(4.9) and $(6.5), respectively	8.1		10.8		
Foreign currency translation	1.8		(0.7		)
Other comprehensive income	12.0		27.5		
Comprehensive income	$	35.4	$	21.3	

See accompanying notes to consolidated financial statements.

Table of Contents

CARPENTER TECHNOLOGY CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
($ in millions)

	Three Months Ended September 30,	
	2017	2016
OPERATING ACTIVITIES		
Net income (loss)	$23.4	$(6.2)
Adjustments to reconcile net income (loss) to net cash (used for) provided from operating activities:		
Depreciation and amortization	28.7	28.9
Deferred income taxes	0.6	37.5
Net pension expense	3.6	16.8
Share-based compensation expense	4.2	3.0
Loss on disposals of property and equipment	0.1	0.1
Changes in working capital and other:		
Accounts receivable	(1.2)	13.2
Inventories	(46.3)	(33.5)
Other current assets	(9.0)	(44.6)
Accounts payable	15.9	(0.7)
Accrued liabilities	(21.7)	(10.5)
Pension plan contributions	(4.2)	—
Other postretirement plan contributions	(0.5)	(1.4)
Other, net	(1.0)	1.5
Net cash (used for) provided from operating activities	(7.4)	4.1
INVESTING ACTIVITIES		
Purchases of property, equipment and software	(28.9)	(26.6)
Net cash used for investing activities	(28.9)	(26.6)
FINANCING ACTIVITIES		
Credit agreement borrowings, net	3.3	—
Dividends paid	(8.6)	(8.5)
Proceeds from stock options exercised	1.4	0.3
Other	(0.2)	(0.2)
Net cash used for financing activities	(4.1)	(8.4)
Effect of exchange rate changes on cash and cash equivalents	(1.0)	(0.2)
DECREASE IN CASH AND CASH EQUIVALENTS	(41.4)	(31.1)
Cash and cash equivalents at beginning of period	66.3	82.0
Cash and cash equivalents at end of period	$24.9	$50.9
SUPPLEMENTAL CASH FLOW INFORMATION:		
Non-cash investing activities:		
Acquisition of property, equipment and software	$9.0	$9.6

See accompanying notes to consolidated financial statements.

Table of Contents

CARPENTER TECHNOLOGY CORPORATION
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2017 AND 2016
(Unaudited)
($ in millions, except per share data)

	Common Stock Par Value Of $5	Common Stock Capital in Excess of Par Value	Reinvested Earnings	Common Stock in Treasury	Accumulated Other Comprehensive (Loss) Income	Total Equity
Balances at June 30, 2017	$276.7	$ 284.8	$1,321.8	$(341.6)	$ (343.1)	$ 1,198.6
Net income			23.4			23.4
Pension and postretirement benefits gain, net of tax					2.1	2.1
Net gain on derivative instruments, net of tax					8.1	8.1
Foreign currency translation					1.8	1.8
Cash Dividends:						0
Common @ $0.18 per share			(8.6)			(8.6)
Share-based compensation plans		4.0		0.2		4.2
Stock options exercised	0.3	1.1				1.4
Balances at September 30, 2017	$277.0	$ 289.9	$1,336.6	$(341.4)	$ (331.1)	$ 1,231.0

	Common Stock Par Value Of $5	Common Stock Capital in Excess of Par Value	Reinvested Earnings	Common Stock in Treasury	Accumulated Other Comprehensive (Loss) Income	Total Equity
Balances at June 30, 2016	$276.3	$ 273.5	$1,308.9	$(343.9)	$ (409.9)	$ 1,104.9
Net loss			(6.2)			(6.2)
Pension and postretirement benefits gain, net of tax					17.4	17.4
Net gain on derivative instruments, net of tax					10.8	10.8
Foreign currency translation					(0.7)	(0.7)
Cash Dividends:						0
Common @ $0.18 per share			(8.5)			(8.5)
Share-based compensation plans		2.6		0.3		2.9
Stock options exercised		0.3				0.3
Balances at September 30, 2016	$276.3	$ 276.4	$1,294.2	$(343.6)	$ (382.4)	$ 1,120.9

See accompanying notes to consolidated financial statements.

Table of Contents
CARPENTER TECHNOLOGY CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments, consisting of normal and recurring adjustments, considered necessary for a fair statement of the results are reflected in the interim periods presented. The June 30, 2017 consolidated balance sheet data was derived from audited financial statements, but does not include all of the disclosures required by accounting principles generally accepted in the United States of America. These unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and footnotes thereto included in Carpenter's annual report on Form 10-K for the fiscal year ended June 30, 2017 (the "2017 Form 10-K"). Operating results for the three months ended September 30, 2017 are not necessarily indicative of the operating results for any future period.

As used throughout this report, unless the context requires otherwise, the terms "Carpenter", the "Company", "Registrant", "Issuer", "we" and "our" refer to Carpenter Technology Corporation.

2. Acquisition and Divestiture

On February 28, 2017, the Company acquired substantially all the assets of Puris LLC ("Puris"), for a cash purchase price of $35.3 million. The acquisition provides the Company with immediate entry into the rapidly growing titanium powder market, an expanded presence in additive manufacturing and strengthens the Company's capabilities as a solutions provider for customers across its end-use markets. The purchase price allocation resulted in the purchase price being allocated as follows: $1.7 million of working capital, $6.5 million of property and equipment, $8.5 million of identifiable intangible assets and $18.6 million to goodwill.

In the fourth quarter of fiscal year 2017, the Company divested the Specialty Steel Supply ("SSS") business. The divestiture was completed in two separate transactions for total cash proceeds of $12.0 million. The operations of the SSS business were historically included in our Performance Engineered Products ("PEP") segment. The Company does not have any significant continuing involvement in the operations of SSS after the divestiture.

3. Earnings per Common Share

The Company calculates basic and diluted earnings per share using the two class method. Under the two class method, earnings are allocated to common stock and participating securities (non-vested restricted shares and units that receive non-forfeitable dividends) according to their participation rights in dividends and undistributed earnings. The earnings available to each class of stock are divided by the weighted average number of outstanding shares for the period in each class. Diluted earnings per share assumes the issuance of common stock for all potentially dilutive share equivalents outstanding. For the three months ended September 30, 2016, the Company incurred a net loss and, accordingly, excluded all potentially dilutive securities from the determination of diluted loss per share as their impact was anti-dilutive.

8

The calculations of basic and diluted earnings (loss) per common share for the three months ended September 30, 2017 and 2016 were as follows:

(in millions, except per share data)	Three Months Ended September 30, 2017	2016
Net income (loss)	$23.4	$(6.2)
Less: earnings and dividends allocated to participating securities	(0.2)	—
Earnings (loss) available for common stockholders used in calculation of basic earnings (loss) per common share	$23.2	$(6.2)
Weighted average number of common shares outstanding, basic	47.1	46.9
Basic earnings (loss) per common share	$0.49	$(0.13)
Net income (loss)	$23.4	$(6.2)
Less: earnings and dividends allocated to participating securities	(0.2)	—
Earnings (loss) available for common stockholders used in calculation of diluted earnings (loss) per common share	$23.2	$(6.2)
Weighted average number of common shares outstanding, basic	47.1	46.9
Effect of shares issuable under share-based compensation plans	0.2	—
Weighted average number of common shares outstanding, diluted	47.3	46.9
Diluted earnings (loss) per common share	$0.49	$(0.13)

The following awards issued under share-based compensation plans were excluded from the above calculations of diluted earnings (loss) per share because their effects were anti-dilutive:

(in millions)	Three Months Ended September 30, 2017	2016
Stock options	1.8	1.8
Restricted stock awards	—	0.1

4. Inventories

Inventories consisted of the following components as of September 30, 2017 and June 30, 2017:

($ in millions)	September 30, 2017	June 30, 2017
Raw materials and supplies	$ 172.0	$ 152.8

Work in process	383.1	365.6
Finished and purchased products	182.2	172.0
Total inventory	$ 737.3	$ 690.4

Inventories are valued at the lower of cost or market. Cost for inventories is principally determined using the last-in, first-out (“LIFO”) inventory costing method. The Company also uses the first-in, first-out (“FIFO”) and average cost methods. As of September 30, 2017 and June 30, 2017, $117.4 million and $107.3 million of inventory, respectively, was accounted for using a method other than the LIFO inventory costing method.

9

Table of Contents
CARPENTER TECHNOLOGY CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

5. Accrued Liabilities

Accrued liabilities consisted of the following as of September 30, 2017 and June 30, 2017:

($ in millions)	September 30, 2017	June 30, 2017
Accrued compensation and benefits	$ 43.3	$ 59.1
Accrued postretirement benefits	15.5	15.5
Deferred revenue	10.2	9.8
Derivative financial instruments	5.8	13.1
Accrued interest expense	5.6	11.2
Accrued income taxes	4.8	5.1
Accrued pension liabilities	3.3	3.3
Other	22.3	22.8
Total accrued liabilities	$ 110.8	$ 139.9

6. Pension and Other Postretirement Benefits

The components of the net periodic benefit cost related to the Company's pension and other postretirement benefits for the three months ended September 30, 2017 and 2016 were as follows:

Three months ended September 30,	Pension Plans		Other Postretirement Plans	
($ in millions)	2017	2016	2017	2016
Service cost	$ 2.4	$ 8.2	$ 0.7	$ 0.9
Interest cost	13.0	13.1	2.4	2.3
Expected return on plan assets	(16.5)	(15.3)	(1.7)	(1.7)
Amortization of net loss	3.4	9.4	0.7	0.8
Amortization of prior service cost (benefit)	0.5	0.2	(1.3)	(1.6)
Curtailment charge	—	0.5	—	—
Net periodic benefit costs	$ 2.8	$ 16.1	$ 0.8	$ 0.7

In September 2016, the Company announced changes to retirement plans it offers to certain employees. Benefits accrued to eligible participants of its largest qualified defined benefit pension plan and certain non-qualified benefit plans were frozen effective December 31, 2016. The Company recognized the plan freeze in the three months ended September 30, 2016 as a curtailment, since the plan changes eliminated the accrual of defined benefits for future services for a significant number of participants. The impact of the curtailment included a one-time accelerated recognition of outstanding unamortized prior service costs of $0.5 million, which was recognized in the three months ended September 30, 2016.

During the three months ended September 30, 2017 and 2016, the Company made $4.2 million and $0.0 million, respectively, of contributions to its qualified defined benefit pension plans. The Company currently expects to contribute $2.6 million to its qualified defined benefit pension plans during the remainder of fiscal year 2018.

7. Debt

On March 31, 2017, the Company entered into a $400.0 million unsecured revolving credit facility ("Credit Agreement") that extends to March 2022. Interest on the borrowings under the Credit Agreement accrue at variable rates, based upon LIBOR or a defined "Base Rate," both are determined based upon the rating of the Company's senior unsecured long-term debt (the "Debt Rating"). The applicable margin to be added to LIBOR ranges from 1.00% to 1.75% (1.50% as of September 30, 2017), and for Base Rate-determined loans, from 0.00% to 0.75% (0.50% as of September 30, 2017). The Company also pays a quarterly commitment fee ranging from 0.125% to 0.400% (0.275% as of September 30, 2017), determined based upon the Debt Rating, of the unused portion of the $400.0 million commitment under the Credit Agreement. In addition, the Company must pay certain letter of credit fees, ranging from 1.00% to 1.75% (1.50% as of September 30, 2017), with respect to letters of credit issued under the Credit Agreement. The Company has the right to voluntarily prepay and re-borrow loans and to terminate or reduce the commitments under the facility. As of September 30, 2017, the Company had $6.1 million of issued letters of credit and $3.3 million of borrowings under the Credit Agreement with the balance of $390.6 million available to the Company.

The Company is subject to certain financial and restrictive covenants under the Credit Agreement, which, among other things, require the maintenance of a minimum interest coverage ratio of 3.50 to 1.00. The interest coverage ratio is defined in the Credit Agreement as, for any period, the ratio of consolidated earnings before interest, taxes, depreciation and amortization and non-cash net pension expense ("EBITDA") to consolidated interest expense for such period. The Credit Agreement also requires the Company to maintain a debt to capital ratio of less than 55 percent. The debt to capital ratio is defined in the Credit Agreement as the ratio of consolidated indebtedness, as defined therein, to consolidated capitalization, as defined therein. As of September 30, 2017 and June 30, 2017, the Company was in compliance with all of the covenants of the Credit Agreement.

Long-term debt outstanding as of September 30, 2017 and June 30, 2017 consisted of the following:

($ in millions)	September 30, 2017	June 30, 2017
Medium-term notes, Series B at 6.97% to 7.10% due from April 2018 to May 2018 (face value of $55.0 million at September 30, 2017 and June 30, 2017)	$ 55.0	$ 55.0
Senior unsecured notes, 5.20% due July 2021 (face value of $250.0 million at September 30, 2017 and June 30, 2017)	250.9	251.2
Senior unsecured notes, 4.45% due March 2023 (face value of $300.0 million at September 30, 2017 and June 30, 2017)	298.9	298.8
Total	604.8	605.0
Less: amounts due within one year	55.0	55.0
Long-term debt, net of current portion	$ 549.8	$ 550.0

For the three months ended September 30, 2017 and 2016, interest costs totaled $7.7 million and $7.5 million, respectively, of which $0.5 million and $0.2 million, respectively, were capitalized as part of the cost of property, equipment and software.

8. Contingencies and Commitments

Environmental

The Company is subject to various federal, state, local and international environmental laws and regulations relating to pollution, protection of public health and the environment, natural resource damages and occupational safety and health. Although compliance with these laws and regulations may affect the costs of the Company's operations, compliance costs to date have not been material. The Company has environmental remediation liabilities at some of its owned operating facilities and has been designated as a potentially responsible party ("PRP") with respect to certain third party Superfund waste-disposal sites and other third party-owned sites. The Company accrues amounts for environmental remediation costs that represent management's best estimate of the probable and reasonably estimable future costs related to environmental remediation. During the three months ended September 30, 2017, no additional accruals were recorded. The liabilities recorded for environmental remediation costs at Superfund sites, other third party-owned sites and Carpenter-owned current or former operating facilities remaining at September 30, 2017 and June 30, 2017 were $16.1 million and $16.1 million, respectively. Additionally, the Company has been notified that it may be a PRP with respect to other Superfund sites as to which no proceedings have been instituted against the Company. Neither the exact amount of remediation costs nor the final method of their allocation among all designated PRPs at these Superfund sites have been determined. Accordingly, at this time, the Company cannot reasonably estimate expected costs for such matters. The liability for future environmental remediation costs that can be reasonably estimated is evaluated by management on a quarterly basis.

Other

The Company is defending various routine claims and legal actions that are incidental to its business and common to its operations, including those pertaining to product claims, commercial disputes, patent infringement, employment actions, employee benefits, compliance with domestic and foreign laws, personal injury claims and tax issues. Like many other manufacturing companies in recent years, the Company, from time to time, has been named as a defendant in lawsuits alleging personal injury as a result of exposure to chemicals and substances in the workplace such as asbestos. The Company provides for costs relating to these matters when a loss is probable and the amount of the loss is reasonably estimable. The effect of the outcome of these matters on the Company's future results of operations and liquidity cannot be predicted because any such effect depends on future results of operations and the amount and timing (both as to recording future charges to operations and cash expenditures) of the resolution of such matters. While it is not feasible to determine the outcome of these matters, management believes that the total liability from these matters will not have a material effect on the Company's financial position, results of operations or cash flows over the long-term. However, there can be no assurance that an increase in the scope of pending matters or that any future lawsuits, claims, proceedings or investigations will not be material to the Company's financial position, results of operations or cash flows in a particular future quarter or year.

9. Fair Value Measurements

The fair value hierarchy has three levels based on the inputs used to determine fair value. Level 1 refers to quoted prices in active markets for identical assets or liabilities. Level 2 refers to observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data. Level 3 refers to unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs. Currently, the Company does not use Level 1 and 3 inputs.

Table of Contents
CARPENTER TECHNOLOGY CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

The following tables present the Company's assets and liabilities that are measured at fair value on a recurring basis and are categorized using the fair value hierarchy:

September 30, 2017	Fair Value Measurements Using Input Type
($ in millions)	Level 2
Assets:	
Marketable securities:	
Municipal auction rate securities	$ 3.4
Derivative financial instruments	14.4
Total assets	$ 17.8
Liabilities:	
Derivative financial instruments	$ 5.9

June 30, 2017	Fair Value Measurements Using Input Type
($ in millions)	Level 2
Assets:	
Marketable securities:	
Municipal auction rate securities	$ 3.4
Derivative financial instruments	14.5
Total assets	$ 17.9
Liabilities:	
Derivative financial instruments	$ 19.1

The Company's derivative financial instruments consist of commodity forward contracts, foreign currency forward contracts and interest rate swaps. These instruments are measured at fair value using the market method valuation technique. The inputs to this technique utilize information related to foreign exchange rates, commodity prices and interest rates published by third party leading financial news and data providers. This is observable data; however, the valuation of these instruments is not based on actual transactions for the same instruments and, as such, they are classified as Level 2. The Company's use of derivatives and hedging policies are more fully discussed in Note 10.

The Company has currently chosen not to elect the fair value option for any items that are not already required to be measured at fair value in accordance with accounting principles generally accepted in the United States of America.

The carrying amounts of other financial instruments not listed in the table below approximate fair value due to the short-term nature of these items. The carrying amounts and estimated fair values of the Company's financial instruments not recorded at fair value in the financial statements were as follows:

	September 30, 2017	June 30, 2017

($ in millions)	Carrying Value	Fair Value	Carrying Value	Fair Value
Long-term debt, including current portion	$604.8	$622.6	$605.0	$622.5
Company-owned life insurance	$15.7	$15.7	$15.9	$15.9

13

The carrying amount of company-owned life insurance reflects cash surrender values based upon the market values of underlying securities, using Level 2 inputs, net of any outstanding policy loans. The carrying value associated with the cash surrender value of these policies is recorded in other assets in the accompanying consolidated balance sheets.

The fair values of long-term debt as of September 30, 2017 and June 30, 2017 were determined by using current interest rates for debt with terms and maturities similar to the Company's existing debt arrangements and accordingly would be classified as Level 2 inputs in the fair value hierarchy.

10. Derivatives and Hedging Activities

The Company uses commodity forwards, interest rate swaps, forward interest rate swaps and foreign currency forwards to manage risks generally associated with commodity price, interest rate and foreign currency rate fluctuations. The following explains the various types of derivatives and includes a recap about the impact the derivative instruments had on the Company's financial position, results of operations and cash flows.

Cash Flow Hedging — Commodity forward contracts: The Company enters into commodity forward contracts to fix the price of a portion of anticipated future purchases of certain critical raw materials and energy to manage the risk of cash flow variability associated with volatile commodity prices. The commodity forward contracts have been designated as cash flow hedges. The qualifying hedge contracts are marked-to-market at each reporting date and any unrealized gains or losses are included in accumulated other comprehensive income (loss) ("AOCI") to the extent effective, and reclassified to cost of sales in the period during which the hedged transaction affects earnings or it becomes probable that the forecasted transaction will not occur. As of September 30, 2017, the Company had forward contracts to purchase 22.2 million pounds of certain raw materials with settlement dates through December 2023.

Cash Flow Hedging — Forward interest rate swaps: Historically, the Company has entered into forward interest rate swap contracts to manage the risk of cash flow variability associated with fixed interest debt expected to be issued. The forward interest rate swaps were designated as cash flow hedges. The qualifying hedge contracts were marked-to-market at each reporting date and any unrealized gains or losses were included in AOCI to the extent effective, and reclassified to interest expense in the period during which the hedged transaction affected earnings or it became probable that the forecasted transaction would not occur. Upon the issuance of the fixed rate debt, the forward interest rate swap contracts were terminated. The realized gains at the time the interest rate swap contracts were terminated are being amortized over the term of the underlying debt. For the three months ended September 30, 2017 and 2016, net gains of $0.1 million and $0.1 million, respectively, related to the previously terminated contracts were recorded as a reduction to interest expense.

Cash Flow Hedging — Foreign currency forward contracts: The Company uses foreign currency forward contracts to hedge a portion of anticipated future sales denominated in foreign currencies, principally the Euro and Pound Sterling, in order to offset the effect of changes in exchange rates. The qualifying hedge contracts are marked-to-market at each reporting date and any unrealized gains or losses are included in AOCI to the extent effective, and reclassified to net sales in the period during which the transaction affects earnings or it becomes probable that the forecasted transaction will not occur.

The Company also uses foreign currency forward contracts to protect certain short-term asset positions denominated in foreign currencies against the effect of changes in exchange rates. These positions do not qualify for hedge accounting and accordingly are marked-to-market at each reporting date through charges to other income and expense.

As of September 30, 2017 and June 30, 2017, the fair value of the outstanding foreign currency forwards not designated as hedging instruments and the charges to income for changes in fair value for these contracts were not material.

Fair Value Hedging - Interest rate swaps: The Company uses interest rate swaps to achieve a level of floating rate debt relative to fixed rate debt where appropriate. The Company has designated fixed to floating interest rate swaps as fair value hedges. Accordingly, the changes in the fair value of these instruments are immediately recorded in earnings. The mark-to-market values of both the fair value hedging instruments and the underlying debt obligations are recorded as equal and offsetting gains and losses in interest expense in the consolidated statements of operations. As of September 30, 2017 and June 30, 2017, the total notional amount of floating interest rate contracts was $150.0 million. For the three months ended September 30, 2017 and 2016, net gains of $0.2 million and $0.4 million, respectively, were recorded as a reduction to interest expense.

Table of Contents

CARPENTER TECHNOLOGY CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

The fair value and location of outstanding derivative contracts recorded in the accompanying consolidated balance sheets were as follows as of September 30, 2017 and June 30, 2017:

September 30, 2017 ($ in millions)	Interest Rate Swaps	Foreign Currency Contracts	Commodity Contracts	Total Derivatives
Asset Derivatives:				
Derivatives designated as hedging instruments:				
Other current assets	$ 0.2	$ 0.6	$ 6.8	$ 7.6
Other assets	1.3	—	5.5	6.8