

BARNES GROUP INC
Form 10-Q
August 02, 2007
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2007

OR

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

For the transition period from _____ to _____

Commission file number 1-4801

BARNES GROUP INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

06-0247840
(I.R.S. Employer
Identification No.)

Edgar Filing: BARNES GROUP INC - Form 10-Q

123 Main Street, Bristol, Connecticut
(Address of Principal Executive Offices)

(860) 583-7070

06011-0489
(Zip Code)

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 No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer

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

The registrant had outstanding 53,533,312 shares of common stock as of July 31, 2007.

Table of Contents

Barnes Group Inc.

Index to Form 10-Q

For the Quarterly Period Ended June 30, 2007

	Page
Part I. <u>FINANCIAL INFORMATION</u>	
Item 1. <u>Financial Statements</u>	
<u>Consolidated Statements of Income for the three months and six months ended June 30, 2007 and 2006</u>	3
<u>Consolidated Balance Sheets as of June 30, 2007 and December 31, 2006</u>	4
<u>Consolidated Statements of Cash Flows for the six months ended June 30, 2007 and 2006</u>	5
<u>Notes to Consolidated Financial Statements</u>	6
<u>Report of Independent Registered Public Accounting Firm</u>	12
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	13
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	20
Item 4. <u>Controls and Procedures</u>	20
Part II. <u>OTHER INFORMATION</u>	
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	21
Item 4. <u>Submission of Matters to a Vote of Security Holders</u>	21
Item 5. <u>Other Information</u>	22
Item 6. <u>Exhibits</u>	22
<u>Signatures</u>	23
<u>Exhibit Index</u>	24

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****BARNES GROUP INC.****CONSOLIDATED STATEMENTS OF INCOME****(Dollars in thousands, except per share data)****(Unaudited)**

	Three months ended June 30,		Six months ended June 30,	
	2007	2006	2007	2006
Net sales	\$ 359,526	\$ 308,927	\$ 720,176	\$ 608,778
Cost of sales	219,832	198,370	440,749	389,003
Selling and administrative expenses	99,399	81,839	195,964	162,950
	319,231	280,209	636,713	551,953
Operating income	40,295	28,718	83,463	56,825
Other income	389	582	631	877
Interest expense	6,489	5,751	13,461	10,138
Other expenses	321	(190)	661	385
Income before income taxes	33,874	23,739	69,972	47,179
Income taxes	5,487	5,721	13,930	10,699
Net income	\$ 28,387	\$ 18,018	\$ 56,042	\$ 36,480
Per common share:				
Net income:				
Basic	\$.53	\$.36	\$ 1.06	\$.74
Diluted	.49	.34	.99	.70
Dividends	.140	.125	.265	.235
Average common shares outstanding:				
Basic	53,134,347	50,401,132	52,855,972	49,334,094
Diluted	57,730,886	52,925,307	56,461,052	51,846,565

See accompanying notes.

Table of Contents**BARNES GROUP INC.****CONSOLIDATED BALANCE SHEETS**

(Dollars in thousands)

(Unaudited)

	June 30, 2007	December 31, 2006
Assets		
Current assets		
Cash and cash equivalents	\$ 22,393	\$ 35,360
Accounts receivable, less allowances (2007 \$5,241; 2006 \$3,589)	222,247	190,775
Inventories	204,065	198,960
Deferred income taxes	22,594	24,923
Prepaid expenses	16,547	11,196
Total current assets	487,846	461,214
Deferred income taxes	27,810	23,544
Property, plant and equipment	585,065	564,987
Less accumulated depreciation	(367,852)	(355,342)
	217,213	209,645
Goodwill	363,512	358,600
Other intangible assets, net	306,102	236,561
Other assets	51,333	46,887
Total assets	\$ 1,453,816	\$ 1,336,451
Liabilities and Stockholders Equity		
Current liabilities		
Notes and overdrafts payable	\$ 10,521	\$ 5,600
Accounts payable	182,344	141,345
Accrued liabilities	106,212	102,951
Long-term debt - current	51,939	45,164
Total current liabilities	351,016	295,060
Long-term debt	377,935	376,318
Accrued retirement benefits	113,495	114,757
Other liabilities	34,690	30,521
Commitments and Contingencies (Note 11)		
Stockholders equity		
Common stock - par value \$0.01 per share		
Authorized: 150,000,000 shares		
Issued: Shares at par value (2007 53,927,151; 2006 52,639,594)	539	526
Additional paid-in capital	210,648	194,210
Treasury stock, at cost (2007 420,324 shares; 2006 230,741 shares)	(9,623)	(4,608)

Edgar Filing: BARNES GROUP INC - Form 10-Q

Retained earnings	392,801	352,823
Accumulated other non-owner changes to equity	(17,685)	(23,156)
Total stockholders' equity	576,680	519,795
Total liabilities and stockholders' equity	\$ 1,453,816	\$ 1,336,451

See accompanying notes.

Table of Contents**BARNES GROUP INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS****(Dollars in thousands)****(Unaudited)**

	Six months ended June 30,	
	2007	2006
Operating activities:		
Net income	\$ 56,042	\$ 36,480
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation and amortization	23,593	19,872
Loss (gain) on disposition of property, plant and equipment	174	(124)
Non-cash stock-based compensation expense	3,955	4,329
Changes in assets and liabilities, net of the effects of acquisitions:		
Accounts receivable	(28,756)	(20,856)
Inventories	(3,307)	(7,749)
Prepaid expenses	(5,186)	(3,899)
Accounts payable	1,739	7,373
Accrued liabilities	(5,124)	(7,598)
Deferred income taxes	4,521	2,037
Long-term retirement benefits	(1,319)	(1,545)
Other	(1,775)	362
Net cash provided by operating activities	44,557	28,682
Investing activities:		
Proceeds from disposition of property, plant and equipment	431	2,237
Capital expenditures	(22,922)	(23,123)
Business acquisitions, net of cash acquired	(1,886)	(96,344)
Revenue sharing program payments	(36,275)	(26,900)
Other	(991)	(882)
Net cash used by investing activities	(61,643)	(145,012)
Financing activities:		
Net change in other borrowings	5,061	(3,430)
Payments on long-term debt	(168,182)	(86,756)
Proceeds from the issuance of long-term debt	176,875	208,052
Proceeds from the issuance of common stock	8,958	22,536
Common stock repurchases		(672)
Dividends paid	(14,053)	(11,774)
Other	(3,636)	(1,174)
Net cash provided by financing activities	5,023	126,782
Effect of exchange rate changes on cash flows	(904)	(988)
(Decrease) increase in cash and cash equivalents	(12,967)	9,464
Cash and cash equivalents at beginning of period	35,360	28,112
Cash and cash equivalents at end of period	\$ 22,393	\$ 37,576

Edgar Filing: BARNES GROUP INC - Form 10-Q

Supplemental Disclosure of Cash Flow Information:

Non-cash financing and investing activities in 2007 and 2006 include the acquisition of \$65.4 million and \$37.8 million, respectively, of intangible assets and the recognition of the corresponding liabilities in connection with the aftermarket revenue sharing programs (RSPs). In 2006, non-cash investing and financing activities included the issuance of \$30.7 million of common stock in connection with the acquisition of Heinz Hänggi GmbH, Stanztechnik.

See accompanying notes.

Table of Contents

BARNES GROUP INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(All dollar amounts included in the notes are stated in thousands except per share data.)

1. Summary of Significant Accounting Policies

The accompanying unaudited consolidated balance sheet and the related consolidated statements of income and cash flows have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. The consolidated financial statements do not include all information and notes required by generally accepted accounting principles for complete financial statements. The balance sheet as of December 31, 2006 has been derived from the 2006 financial statements of Barnes Group Inc. (the Company). For additional information, please refer to the consolidated financial statements and notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2006. In the opinion of management, all adjustments, including normal recurring accruals considered necessary for a fair presentation, have been included. Operating results for the six-month period ended June 30, 2007 are not necessarily indicative of the results that may be expected for the year ending December 31, 2007. Certain reclassifications have been made to prior year amounts to conform to the current year presentation.

See Note 9 for discussion of the impact of the Company's adoption of Financial Accounting Standards Board (FASB) Interpretation (FIN) No. 48, Accounting for Uncertainty in Income Taxes, on January 1, 2007.

2. Net Income Per Common Share

For the purpose of computing diluted net income per share, the weighted-average number of shares outstanding was increased by 4,596,539 and 2,524,175 for the three-month periods ended June 30, 2007 and 2006, respectively, and 3,605,080 and 2,512,471 for the six-month periods ended June 30, 2007 and 2006, respectively, to account for the potential dilutive effects of stock-based incentive plans and convertible senior subordinated notes.

As of June 30, 2007, there were 5,102,602 options for shares of common stock outstanding of which 5,023,102 were considered dilutive. As of June 30, 2006, there were 5,088,626 options for shares of common stock outstanding of which 4,782,726 were considered dilutive. There were no adjustments to net income for the purpose of computing income available to common stockholders for those periods.

The Company granted 677,150 stock options (675,450 after forfeitures) and 151,474 restricted stock unit awards in February, 2007 as part of its annual award grant. Of the 151,474 restricted stock unit awards, 70,500 vest upon satisfying established performance goals.

The Company had 186,000 restricted stock unit awards which had accelerated vesting provisions based upon meeting market conditions as defined in the award agreements. During the second quarter of 2007, the vesting acceleration conditions of these rights were satisfied. As a result, fifty percent of the restricted stock units (93,000 units) vested on June 20, 2007 and the remaining 50% (93,000 units) will vest on June 20, 2008.

As discussed in Note 7, the convertible senior subordinated notes due in August, 2025 (the 3.75% Convertible Notes) are convertible, under certain circumstances, into a combination of cash and common stock of the Company. The conversion price as of June 30, 2007 was approximately \$21.01 per share of common stock. As of June 30, 2007, the Company's market price per share exceeded the conversion price of the notes. Under the net share settlement method, there were 1,548,163 and 913,789 potential shares issuable under the notes that were considered dilutive for the three- and six-month periods ended June 30, 2007, respectively.

As discussed in Note 7, in March, 2007, the Company sold \$100,000 of convertible senior subordinated notes due March, 2027 (the 3.375% Convertible Notes). These notes are convertible, under certain circumstances, into a combination of cash and common stock of the Company. The conversion price as of June 30, 2007 was approximately \$28.68 per share of common stock. As of June 30, 2007, the Company's market price per share exceeded the conversion price of the notes. Under the net share settlement method, there were 275,275 and 137,637 potential shares issuable under these notes that were considered dilutive for the three- and six-month periods ended June 30, 2007, respectively.

Table of Contents**3. Acquisitions**

During 2006, the Company acquired three businesses, Heinz Hänggi GmbH, Stanztechnik (Heinz Hänggi), the KENT division of Premier Farnell (KENT) and the Nitropush product line of Orflam Industries of France (Nitropush). The following table reflects the unaudited pro forma operating results of the Company for the three months and six months ended June 30, 2006, which give effect to the acquisitions as if they had occurred on January 1, 2006. The pro forma results are based on assumptions that the Company believes are reasonable under the circumstances. The pro forma results are not necessarily indicative of the operating results that would have occurred if the acquisitions had been effective January 1, 2006 nor are they intended to be indicative of results that may occur in the future. The underlying pro forma information includes the historical financial results of the Company, Heinz Hänggi, KENT and Nitropush adjusted for certain items including depreciation and amortization expense associated with the assets acquired and the Company's financing arrangements. The pro forma information does not include the effects of any synergies or cost reduction initiatives related to the acquisitions.

	Three months ended June 30, 2006	Six months ended June 30, 2006
Net sales	\$ 333,783	\$ 662,477
Income before income taxes	27,523	52,681
Net income	20,812	40,348
Net income per common share:		
Basic	\$ 0.41	\$ 0.80
Diluted	0.39	0.76

4. Comprehensive Income

Comprehensive income includes all changes in equity during a period except those resulting from the investments by, and distributions to, stockholders. For the Company, comprehensive income for the period includes net income and other non-owner changes to equity, net of taxes.

Statements of Comprehensive Income**(Unaudited)**

	Three months ended June 30,		Six months ended June 30,	
	2007	2006	2007	2006
Net income	\$ 28,387	\$ 18,018	\$ 56,042	\$ 36,480
Unrealized gains (losses) on hedging activities	(174)	117	(119)	116
Foreign currency translation adjustments	3,518	6,966	4,168	9,546
Defined benefit pension and other postretirement plans	348		1,422	
Comprehensive income	\$ 32,079	\$ 25,101	\$ 61,513	\$ 46,142

Defined benefit pension and other postretirement plans reflects the amortization of prior service costs and recognized losses related to such plans during the periods as a result of the adoption of Statement of Financial Accounting Standards (SFAS) No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, in the fourth quarter of 2006.

Table of Contents**5. Inventories**

The components of inventories were:

	June 30, 2007	December 31, 2006
Finished goods	\$ 122,378	\$ 123,460
Work-in-process	46,912	42,898
Raw material and supplies	34,775	32,602
	\$ 204,065	\$ 198,960

6. Goodwill and Other Intangible Assets**Goodwill:**

The following table sets forth the change in the carrying amount of goodwill for each reportable segment and for the Company for the period ended June 30, 2007:

	Barnes Aerospace	Barnes Distribution	Barnes Industrial	Total Company
January 1, 2007	\$ 30,786	\$ 156,745	\$ 171,069	\$ 358,600
Goodwill acquired, net of adjustments		3,568	(952)	2,616
Foreign currency translation		3,277	(981)	2,296
June 30, 2007	\$ 30,786	\$ 163,590	\$ 169,136	\$ 363,512

Goodwill recorded at Barnes Distribution increased in 2007 as a result of the recognition of \$1,830 of assumed liabilities related to the KENT acquisition. The purchase price allocation of the KENT acquisition is subject to the finalization of the valuation of certain assets and liabilities and, thus, these preliminary values are subject to revision. Additionally, during 2007, goodwill recorded at Barnes Distribution was increased as a result of the contingent purchase price adjustments of £0.8 million (approximately \$1,600 U.S. Dollars) for the achievement of certain performance targets related to the 2005 Toolcom acquisition.

The changes in goodwill recorded at Barnes Industrial, formerly known as Associated Spring, resulted primarily from adjustments to the valuation of certain assets and liabilities related to the 2006 acquisition of Heinz Hänggi. The purchase price allocation of the Heinz Hänggi acquisition was finalized during the second quarter of 2007.

Other Intangible Assets:

Other intangible assets consisted of:

		June 30, 2007		December 31, 2006	
	Range of Life - Years	Gross Amount	Accumulated Amortization	Gross Amount	Accumulated Amortization
Amortized intangible assets:					
Revenue sharing programs	Up to 30	\$ 264,700	\$ (8,127)	\$ 190,200	\$ (5,359)
Customer lists/relationships	10	28,578	(7,606)	28,333	(6,160)
Patents, trademarks/trade names	5-30	25,148	(5,319)	24,974	(4,247)

Edgar Filing: BARNES GROUP INC - Form 10-Q

Other	Up to 15	8,262	(1,858)	8,262	(1,576)
		326,688	(22,910)	251,769	(17,342)
Foreign currency translation		2,324		2,134	
Other intangible assets		\$ 329,012	\$ (22,910)	\$ 253,903	\$ (17,342)

Table of Contents

Amortization of intangible assets is expected to increase from approximately \$11,100 in 2007 to \$14,700 in 2011.

During the first half of 2007, the Company entered into additional aftermarket RSP agreements with a major aerospace customer, General Electric Company (General Electric), under which the Company is the sole supplier of certain aftermarket parts to this customer. As consideration for these agreements, the Company agreed to pay participation fees of \$74,500 of which \$9,125 has been paid, \$36,875 will be paid in the second half of 2007 and \$28,500 will be paid during the first quarter of 2008.

7. Debt

In March, 2007, the Company sold \$100,000 of convertible senior subordinated notes due 2027 bearing interest at a fixed rate of 3.375%. The net proceeds from the offering were used to repay outstanding indebtedness under the Company's revolving credit facility. The 3.375% Convertible Notes are general unsecured obligations of the Company and are subordinated in right of payment to all existing and future senior debt of the Company. These notes are subject to redemption at their par value at any time, at the option of the Company, on or after March 20, 2014. These notes may be converted under certain circumstances, into a combination of cash and common stock of the Company at a conversion value equal to 34.8646 shares per note, equivalent to a conversion price of approximately \$28.68 per share of common stock as of June 30, 2007. The first \$1 of the conversion value of each note would be paid in cash and the additional conversion value, if any, would be paid in cash or common stock, at the option of the Company.

In July 2007, the Company delivered a notice to holders of the 3.75% Convertible Notes due 2025 that from July 1, 2007 until September 30, 2007, the 3.75% Convertible Notes are eligible for conversion as provided in the indenture relating to such notes. As a result of these notes becoming eligible for conversion, the Company will record a non-cash pretax charge of approximately \$2,400 in the third quarter of 2007 to expense the remaining unamortized deferred debt issuance costs related to these notes. The Company continued to classify these notes as non-current as the Company has both the intent and ability, through its revolving credit facility, to refinance these notes on a long-term basis.

8. Pension and Other Postretirement Benefits

Pension and other postretirement benefits expenses consisted of the following:

	Three months ended June 30,		Six months ended June 30,	
	2007	2006	2007	2006
Pensions				
Service cost	\$ 2,001	\$ 3,115	\$ 4,048	\$ 6,266
Interest cost	5,449	5,242	10,779	10,497
Expected return on plan assets	(7,574)	(7,743)	(15,286)	(15,558)
Amortization of transition assets		(1)		(1)
Amortization of prior service cost	369	397	742	794
Recognized losses	568	542	1,079	1,121
Curtailement gain	(84)		(84)	
Special termination benefits		26		26
Net periodic benefit cost	\$ 729	\$ 1,578	\$ 1,278	\$ 3,145

	Three months ended June 30,		Six months ended June 30,	
	2007	2006	2007	2006
Other Postretirement Benefits				
Service cost	\$ 254	\$ 338	\$ 558	\$ 1,087
Interest cost	1,113	1,084	2,265	2,172
Amortization of prior service cost	302	226	592	451
Recognized losses	158	238	364	474

Edgar Filing: BARNES GROUP INC - Form 10-Q

Net periodic benefit cost	\$ 1,827	\$ 1,886	\$ 3,779	\$ 4,184
---------------------------	----------	----------	----------	----------

Table of Contents**9. Income Taxes**

The Company adopted the provisions of FIN No. 48, Accounting for Uncertainty in Income Taxes, on January 1, 2007. As a result of the implementation of FIN No. 48, the Company recorded an adjustment of \$1,688 for unrecognized tax benefits which was accounted for as a reduction to the January 1, 2007 retained earnings balance. As of January 1, 2007, the total amount of unrecognized tax benefits recorded in the statement of financial position in accordance with this Interpretation is \$9,399, of which \$8,219, if recognized, would impact the effective tax rate.

The Company recognizes accrued interest related to unrecognized tax benefits and penalties in income tax expense. Approximately \$310 is included in the unrecognized tax benefits recorded as of January 1, 2007, for the payment of interest and a minimal amount for penalties associated with those positions.

The Company or its subsidiaries file income tax returns in the U.S. federal jurisdiction, and various state and foreign jurisdictions. In the normal course of business, the Company is subject to examination by various taxing authorities, including the Internal Revenue Service in the U.S. (the IRS) and the taxing authorities in other major jurisdictions such as Canada, France, Germany, Singapore, Sweden, Switzerland and the United Kingdom. With few exceptions, the Company is no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for years before 2003.

In connection with an IRS audit for the tax years 2000 through 2002, the IRS proposed adjustments to these tax years of approximately \$16,500, plus a potential penalty of 20% of the tax assessment plus interest. These adjustments related to foreign income inclusion of certain foreign subsidiaries. The Company filed an administrative protest of these adjustments and is currently engaged in discussions with the Appeals office of the IRS. The Company and its advisors believe the Company's tax position on the issues raised by the IRS is correct and, therefore, the Company will continue to vigorously defend its position. The Company and its advisors believe the Company will prevail on this issue. It is the Company's belief that the two parties could come to resolution of these issues within the next 12 months. Any additional impact on the Company's liability for income taxes cannot presently be determined, but the Company believes it is adequately provided for and the outcome will not have a material impact on its results of operations, financial position or cash flows.

10. Information on Business Segments

The following table sets forth information about the Company's operations by its three reportable business segments:

	Three months ended		Six months ended	
	June 30,		June 30,	
	2007	2006	2007	2006
Net sales				
Barnes Aerospace	\$ 92,418	\$ 73,920	\$ 183,610	\$ 140,863
Barnes Distribution	150,683	125,507	303,186	249,899
Barnes Industrial	118,707	112,118	238,277	223,108
Intersegment sales	(2,282)	(2,618)	(4,897)	(5,092)
Total net sales	\$ 359,526	\$ 308,927	\$ 720,176	\$ 608,778
Operating profit				
Barnes Aerospace	\$ 18,582	\$ 10,622	\$ 35,424	\$ 19,168
Barnes Distribution	7,475	8,871	17,639	17,824
Barnes Industrial	14,266	9,213	30,455	19,843
Total operating profit	40,323	28,706	83,518	56,835
Interest income	251	322	439	562
Interest expense	(6,489)	(5,751)	(13,461)	(10,138)
Other income (expense), net	(211)	462	(524)	(80)
Total income before income taxes	\$ 33,874	\$ 23,739	\$ 69,972	\$ 47,179

Table of Contents

The aftermarket RSP agreements entered into in 2007 added \$74,500 of intangible assets to the Barnes Aerospace segment assets.

In the third quarter of 2007, the Company is realigning its reportable business segments by transferring the Raymond division, the stock spring catalog and custom solutions business, from Barnes Distribution to Barnes Industrial, whose Associated Spring division manufactures many of the spring products sold by the business. Segment information will be adjusted on a retrospective basis to reflect this change beginning in the third quarter of 2007.

11. Commitments and Contingencies Product Warranties

The Company provides product warranties in connection with the sale of products. From time to time, the Company is subject to customer claims with respect to product warranties. Product warranty liabilities were not significant as of June 30, 2007.

Contingent Payments

In connection with the Toolcom Supplies Ltd. acquisition in August, 2005, approximately £2.2 million of the purchase price were payable within two years of the closing date, contingent upon the occurrence of certain events or the achievement of certain performance targets. In 2007 and 2006, £0.8 million (approximately \$1,600) and £0.9 million (approximately \$1,700) were earned and paid, respectively. The remaining balance of £0.6 million (approximately \$1,100) will be recorded if and when paid.

In connection with the Service Plus Distributors, Inc. acquisition in September, 2005, \$3,700 of the purchase price could be earned within three years of the closing date, contingent upon the occurrence of certain events or the achievement of certain performance targets. In 2006, \$1,500 was earned and paid. The remaining balance of \$2,200 will be recorded if and when paid.

Income Taxes

See Note 9 for contingencies related to income taxes.

With respect to the unaudited consolidated financial information of Barnes Group Inc. for the three-month and six-month periods ended June 30, 2007 and 2006, PricewaterhouseCoopers LLP reported that they have applied limited procedures in accordance with professional standards for a review of such information. However, their separate report dated August 1, 2007 appearing herein, states that they did not audit and they do not express an opinion on that unaudited consolidated financial information. PricewaterhouseCoopers LLP has not carried out any significant or additional tests beyond those that would have been necessary if their report had not been included. Accordingly, the degree of reliance on their report should be restricted in light of the limited nature of the review procedures applied. PricewaterhouseCoopers LLP is not subject to the liability provisions of Section 11 of the Securities Act of 1933, as amended, for their report on the unaudited consolidated financial information because that report is not a report or a part of the registration statement prepared or certified by PricewaterhouseCoopers LLP within the meaning of Sections 7 and 11 of the Securities Act of 1933, as amended.

Table of Contents

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of

Barnes Group Inc.

We have reviewed the accompanying consolidated balance sheet of Barnes Group Inc. and its subsidiaries as of June 30, 2007 and the related consolidated statements of income for each of the three-month and six-month periods ended June 30, 2007 and 2006 and the consolidated statements of cash flows for the six-month periods ended June 30, 2007 and 2006. This interim financial information is the responsibility of the Company's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying consolidated interim financial information for it to be in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 9 to the consolidated financial information, the Company adopted Financial Accounting Standards Board Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* an interpretation of FASB Statement No. 109, effective January 1, 2007.

We previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of December 31, 2006, and the related consolidated statements of income, of changes in stockholders' equity and of cash flows for the year then ended (not presented herein), and in our report dated February 23, 2007, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet information as of December 31, 2006 is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

/s/ PricewaterhouseCoopers LLP
PricewaterhouseCoopers LLP
Hartford, Connecticut
August 1, 2007

Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**
OVERVIEW

Please refer to the Overview found in the Management's Discussion and Analysis of Financial Condition and Results of Operations in the Company's Annual Report on Form 10-K for the year ended December 31, 2006. This Overview sets forth key management objectives and key performance indicators used by management as well as key industry and economic data tracked by management.

As discussed in Note 10 of the Notes to the Consolidated Financial Statements of this Quarterly Report on Form 10-Q, the Company is realigning its reportable business segments in the third quarter of 2007 by transferring the stock spring catalog and custom solutions business from Barnes Distribution to Barnes Industrial, whose Associated Spring division manufactures many of the spring products sold by the business. All previously reported segment information will be adjusted on a retrospective basis to reflect this change beginning in the third quarter of 2007.

Second Quarter 2007 Highlights

In the second quarter, the Company achieved record sales of \$359.5 million, an increase of 16.4% over 2006, driven by a combination of organic growth, primarily in Barnes Aerospace, and incremental sales from recent acquisitions. Operating income improved 40.3% as a result of profitable sales growth and operational improvements.

Barnes Aerospace added to its aftermarket RSP investment by entering into an additional aftermarket RSP agreement with General Electric, further expanding its long-term position for aftermarket sales of aircraft engine parts.

Management initiated Project Catalyst to accelerate the pace of improvement within Barnes Distribution. Project Catalyst consists of four initiatives; global product sourcing, logistics and network optimization, sales and margin improvement, and European market development, including the KENT integration. Costs associated with Project Catalyst in the second quarter of 2007 were approximately \$2.0 million.

RESULTS OF OPERATIONS**Sales**

<i>(in millions)</i>	Three months ended June 30,				Six months ended June 30,			
	2007	2006	Change		2007	2006	Change	
Barnes Aerospace	\$ 92.4	\$ 73.9	\$ 18.5	25.0%	\$ 183.6	\$ 140.9	\$ 42.7	30.3%
Barnes Distribution	150.7	125.5	25.2	20.1%	303.2	249.9	53.3	21.3%
Barnes Industrial	118.7	112.1	6.6	5.9%	238.3	223.1	15.2	6.8%
Intersegment sales	(2.3)	(2.6)	0.3	12.9%	(4.9)	(5.1)	0.2	3.8%
Total	\$ 359.5	\$ 308.9	\$ 50.6	16.4%	\$ 720.2	\$ 608.8	\$ 111.4	18.3%

The Company reported net sales of \$359.5 million in the second quarter of 2007, an increase of \$50.6 million or 16.4%, over the second quarter of 2006. The sales increase reflected \$19.9 million of organic sales growth primarily at Barnes Aerospace, including sales from the aftermarket RSPs. Additionally, the 2006 acquisitions of KENT and Heinz Hänggi contributed \$22.2 million and \$4.2 million of incremental sales to the Barnes Distribution and Barnes Industrial segments, respectively. Foreign currency translation favorably impacted sales by \$4.3 million in 2007 as foreign currencies strengthened against the U.S. Dollar, primarily in Europe.

Sales for the six-month period ended June 30, 2007 were \$720.2 million, an increase of \$111.4 million, or 18.3%, over the 2006 period driven by \$45.3 million of organic sales growth and \$57.8 million from acquisitions. KENT added \$44.9 million of incremental sales to the Barnes Distribution segment while the Heinz Hänggi acquisition contributed \$12.9 million of incremental sales to the Barnes Industrial segment. Foreign currency translation favorably impacted sales by \$8.3 million in 2007 as foreign currencies strengthened against the U.S. Dollar, primarily in Europe.

Table of Contents

Expenses and Operating Income

<i>(in millions)</i>	Three months ended			Six months ended June 30,
	2007	2006	Change	