

MOHAWK INDUSTRIES INC

Form 10-Q

August 05, 2011

[Table of Contents](#)

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

[Mark One]

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

For the quarterly period ended July 2, 2011

OR

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

For the transition period from            to

Commission File Number

01-13697

**MOHAWK INDUSTRIES, INC.**

Edgar Filing: MOHAWK INDUSTRIES INC - Form 10-Q

(Exact name of registrant as specified in its charter)

<b>Delaware</b> (State or other jurisdiction of incorporation or organization)	<b>52-1604305</b> (I.R.S. Employer Identification No.)
<b>160 S. Industrial Blvd., Calhoun, Georgia</b> (Address of principal executive offices)	<b>30701</b> (Zip Code)
<b>Registrant's telephone number, including area code: (706) 629-7721</b>	

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 checked="" type="checkbox"/>	Accelerated filer <input 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 ☒

The number of shares outstanding of the issuer's classes of common stock as of July 29, 2011, the latest practicable date, is as follows:  
68,758,713 shares of Common Stock, \$.01 par value.

**Table of Contents**

**MOHAWK INDUSTRIES, INC.**

**INDEX**

	Page No
Part I.	
<b><u>FINANCIAL INFORMATION</u></b>	
Item 1.	
<b><u>Financial Statements</u></b>	
<b><u>Condensed Consolidated Balance Sheets as of July 2, 2011 and December 31, 2010</u></b>	3
<b><u>Condensed Consolidated Statements of Operations for the three months ended July 2, 2011 and July 3, 2010</u></b>	5
<b><u>Condensed Consolidated Statements of Operations for the six months ended July 2, 2011 and July 3, 2010</u></b>	6
<b><u>Condensed Consolidated Statements of Cash Flows for the six months ended July 2, 2011 and July 3, 2010</u></b>	7
<b><u>Notes to Condensed Consolidated Financial Statements</u></b>	8
Item 2.	
<b><u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u></b>	18
Item 3.	
<b><u>Quantitative and Qualitative Disclosures About Market Risk</u></b>	26
Item 4.	
<b><u>Controls and Procedures</u></b>	26
Part II.	
<b><u>OTHER INFORMATION</u></b>	
Item 1.	
<b><u>Legal Proceedings</u></b>	27
Item 1A.	
<b><u>Risk Factors</u></b>	27
Item 2.	
<b><u>Unregistered Sales of Equity Securities and Use of Proceeds</u></b>	34
Item 3.	
<b><u>Defaults Upon Senior Securities</u></b>	34
Item 4.	
<b><u>(Removed and Reserved)</u></b>	34
Item 5.	
<b><u>Other Information</u></b>	34
Item 6.	
<b><u>Exhibits</u></b>	34

**Table of Contents**

PART I. FINANCIAL INFORMATION

ITEM I. FINANCIAL STATEMENTS

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

ASSETS

(In thousands)

(Unaudited)

	July 2, 2011	December 31, 2010
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 285,422	354,217
Restricted cash		27,954
Receivables, net	797,893	614,473
Inventories	1,102,769	1,007,503
Prepaid expenses	103,518	91,731
Deferred income taxes	135,338	133,304
Other current assets	22,297	19,431
Total current assets	2,447,237	2,248,613
Property, plant and equipment, at cost	3,649,881	3,518,392
Less accumulated depreciation and amortization	1,918,967	1,831,268
Property, plant and equipment, net	1,730,914	1,687,124
Goodwill	1,418,830	1,369,394
Tradenames	481,351	456,890
Other intangible assets, net	199,827	220,237
Deferred income taxes and other non-current assets	110,841	116,668
	\$ 6,389,000	6,098,926

See accompanying notes to condensed consolidated financial statements.

**Table of Contents**

## MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED BALANCE SHEETS

## LIABILITIES AND STOCKHOLDERS' EQUITY

(In thousands, except per share data)

(Unaudited)

	July 2, 2011	December 31, 2010
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Current portion of long-term debt	\$ 453,185	350,588
Accounts payable and accrued expenses	771,297	698,326
<b>Total current liabilities</b>	<b>1,224,482</b>	<b>1,048,914</b>
Deferred income taxes	366,610	346,503
Long-term debt, less current portion	1,155,150	1,302,994
Other long-term liabilities	93,499	93,518
<b>Total liabilities</b>	<b>2,839,741</b>	<b>2,791,929</b>
Commitments and contingencies (Notes 12 and 13)		
Redeemable noncontrolling interest	32,300	35,441
Stockholders' equity:		
Preferred stock, \$.01 par value; 60 shares authorized; no shares issued		
Common stock, \$.01 par value; 150,000 shares authorized; 79,792 and 79,666 shares issued in 2011 and 2010, respectively	798	797
Additional paid-in capital	1,242,963	1,235,445
Retained earnings	2,265,188	2,180,843
Accumulated other comprehensive income, net	331,558	178,097
	3,840,507	3,595,182
Less treasury stock at cost; 11,035 and 11,037 shares in 2011 and 2010, respectively	323,548	323,626
<b>Total stockholders' equity</b>	<b>3,516,959</b>	<b>3,271,556</b>
	<b>\$ 6,389,000</b>	<b>6,098,926</b>

See accompanying notes to condensed consolidated financial statements.

**Table of Contents**

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(Unaudited)

	Three Months Ended	
	July 2, 2011	July 3, 2010
Net sales	\$ 1,477,854	1,400,086
Cost of sales	1,095,607	1,025,330
Gross profit	382,247	374,756
Selling, general and administrative expenses	280,547	285,030
Operating income	101,700	89,726
Other expense (income):		
Interest expense	25,760	39,031
Other expense	2,963	3,675
Other income	(2,567)	(3,131)
	26,156	39,575
Earnings before income taxes	75,544	50,151
Income tax expense (benefit)	13,450	(18,814)
Net earnings	62,094	68,965
Less: Net earnings attributable to noncontrolling interest	1,191	884
Net earnings attributable to Mohawk Industries, Inc.	\$ 60,903	68,081
Basic earnings per share attributable to Mohawk Industries, Inc.	\$ 0.89	0.95
Diluted earnings per share attributable to Mohawk Industries, Inc.	\$ 0.88	0.95

See accompanying notes to condensed consolidated financial statements.

**Table of Contents**

## MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(Unaudited)

	Six Months Ended	
	July 2, 2011	July 3, 2010
Net sales	\$ 2,821,449	2,747,322
Cost of sales	2,097,610	2,031,320
Gross profit	723,839	716,002
Selling, general and administrative expenses	566,055	572,655
Operating income	157,784	143,347
Other expense (income):		
Interest expense	52,355	72,939
Other expense	6,193	3,837
Other income	(5,812)	(7,824)
	52,736	68,952
Earnings before income taxes	105,048	74,395
Income tax expense (benefit)	18,416	(15,840)
Net earnings	86,632	90,235
Less: Net earnings attributable to noncontrolling interest	2,287	1,616
Net earnings attributable to Mohawk Industries, Inc.	\$ 84,345	88,619
Basic earnings per share attributable to Mohawk Industries, Inc.	\$ 1.23	1.25
Diluted earnings per share attributable to Mohawk Industries, Inc.	\$ 1.22	1.24

See accompanying notes to condensed consolidated financial statements.

**Table of Contents**

## MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Six Months Ended	
	July 2, 2011	July 3, 2010
Cash flows from operating activities:		
Net earnings	\$ 86,632	90,235
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Restructuring	13,327	8,933
Depreciation and amortization	148,597	149,295
Deferred income taxes	331	(18,338)
Loss on extinguishment of debt		7,514
Loss (gain) on disposal of property, plant and equipment	485	(952)
Excess tax benefit from stock-based compensation		(162)
Stock-based compensation expense	6,038	3,484
Changes in operating assets and liabilities:		
Receivables, net	(164,107)	(117,129)
Income tax receivable		79,776
Inventories	(84,776)	(82,901)
Accounts payable and accrued expenses	30,522	(12,240)
Other assets and prepaid expenses	(7,193)	(10,308)
Other liabilities	(1,266)	(8,230)
Net cash provided by operating activities	28,590	88,977
Cash flows from investing activities:		
Additions to property, plant and equipment	(112,519)	(47,139)
Net cash used in investing activities	(112,519)	(47,139)
Cash flows from financing activities:		
Payments on revolving line of credit	(637,430)	
Proceeds from revolving line of credit	890,430	
Repayment of senior notes	(298,248)	(199,992)
Borrowings (payments) on term loan and other debt	(125)	188
Debt extinguishment costs		(7,514)
Distribution to noncontrolling interest	(5,428)	(2,668)
Change in restricted cash	27,954	
Excess tax benefit from stock-based compensation		162
Change in outstanding checks in excess of cash	16,788	(3,229)
Proceeds from stock transactions	2,646	1,013
Net cash used in financing activities	(3,413)	(212,040)
Effect of exchange rate changes on cash and cash equivalents	18,547	(18,583)
Net change in cash and cash equivalents	(68,795)	(188,785)
Cash and cash equivalents, beginning of period	354,217	531,458



## Edgar Filing: MOHAWK INDUSTRIES INC - Form 10-Q

Cash and cash equivalents, end of period	\$ 285,422	342,673
------------------------------------------	------------	---------

See accompanying notes to condensed consolidated financial statements.

**Table of Contents**

## MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

## 1. Interim reporting

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with instructions to Form 10-Q and do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. These statements should be read in conjunction with the consolidated financial statements and notes thereto, and the Company's description of critical accounting policies, included in the Company's 2010 Annual Report on Form 10-K, as filed with the Securities and Exchange Commission.

## 2. New pronouncements

In June 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2011-05, *Comprehensive Income (Topic 220) Presentation of Comprehensive Income* (ASU 2011-05). This update requires that the components of net income, the components of other comprehensive income and the total of comprehensive income be presented as a single continuous financial statement or in two separate but consecutive statements. The option of presenting other comprehensive income in the statement of stockholders' equity is eliminated. This update also requires the presentation on the face of the financial statements of reclassification adjustments for items that are reclassified from other comprehensive income to net income in the statements where the components of net income and the components of other comprehensive income are presented. ASU 2011-05 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011.

## 3. Receivables, net

Receivables, net are as follows:

	July 2, 2011	December 31, 2010
Customers, trade	\$ 807,317	621,539
Income tax receivable	10,804	11,027
Other	27,367	27,662
	845,488	660,228
Less allowance for discounts, returns, claims and doubtful accounts	47,595	45,755
Receivables, net	\$ 797,893	614,473

## 4. Inventories

The components of inventories are as follows:

Edgar Filing: MOHAWK INDUSTRIES INC - Form 10-Q

	July 2, 2011	December 31, 2010
Finished goods	\$ 675,600	624,082
Work in process	98,282	97,257
Raw materials	328,887	286,164
Total inventories	\$ 1,102,769	1,007,503

**Table of Contents**

## MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

## 5. Goodwill and intangible assets

The components of goodwill and other intangible assets are as follows:

	Mohawk	Dal-Tile	Unilin	Total
Balances as of December 31, 2010				
Goodwill	\$ 199,132	1,186,913	1,310,774	2,696,819
Accumulated impairments losses	(199,132)	(531,930)	(596,363)	(1,327,425)
		654,983	714,411	1,369,394
Currency translation during the period			49,436	49,436
Balances as of July 2, 2011				
Goodwill	199,132	1,186,913	1,360,210	2,746,255
Accumulated impairments losses	(199,132)	(531,930)	(596,363)	(1,327,425)
	\$	654,983	763,847	1,418,830

	Tradenames
<b>Indefinite life assets not subject to amortization:</b>	
Balance as of December 31, 2010	\$ 456,890
Currency translation during the period	24,461
Balance as of July 2, 2011	\$ 481,351

	Customer relationships	Patents	Other	Total
<b>Intangible assets subject to amortization:</b>				
Balance as of December 31, 2010	\$ 106,432	112,520	1,285	220,237
Amortization during the period	(23,799)	(11,514)	(61)	(35,374)
Currency translation during the period	4,875	10,076	13	14,964
Balance as of July 2, 2011	\$ 87,508	111,082	1,237	199,827

Three Months Ended

Six Months Ended

# Edgar Filing: MOHAWK INDUSTRIES INC - Form 10-Q

	July 2, 2011	July 3, 2010	July 2, 2011	July 3, 2010
Amortization expense	\$ 17,975	16,762	35,374	34,980

## 6. Accounts payable and accrued expenses

	July 2, 2011	December 31, 2010
Outstanding checks in excess of cash	\$ 16,788	
Accounts payable, trade	416,909	353,387
Accrued expenses	157,127	147,595
Product warranties	32,052	37,265
Accrued interest	36,938	45,696
Income taxes payable	4,373	9,301
Deferred tax liability	7,894	5,089
Accrued compensation and benefits	99,216	99,993
Total accounts payable and accrued expenses	\$ 771,297	698,326

## Table of Contents

### MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

#### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

#### 7. Product warranties

The Company warrants certain qualitative attributes of its products for up to 50 years. The Company records a provision for estimated warranty and related costs in accrued expenses, based on historical experience, and periodically adjusts these provisions to reflect actual experience.

The provision for warranty obligations is as follows:

	Three Months Ended		Six Months Ended	
	July 2, 2011	July 3, 2010	July 2, 2011	July 3, 2010
Balance at beginning of period	\$ 36,437	53,450	37,265	66,545
Warranty claims paid during the period	(17,012)	(18,751)	(30,747)	(43,124)
Pre-existing warranty accrual adjustment during the period	489		3,484	
Warranty expense during the period	12,138	9,802	22,050	21,080
Balance at end of period	\$ 32,052	44,501	32,052	44,501

#### 8. Comprehensive income (loss)

Comprehensive income (loss) is as follows:

	Three Months Ended		Six Months Ended	
	July 2, 2011	July 3, 2010	July 2, 2011	July 3, 2010
Net earnings	\$ 62,094	68,965	86,632	90,235
Other comprehensive income (loss):				
Foreign currency translation	38,730	(113,126)	153,461	(213,113)
Comprehensive income (loss)	100,824	(44,161)	240,093	(122,878)
Comprehensive income attributable to the noncontrolling interest	(1,191)	(884)	(2,287)	(1,616)
Comprehensive income (loss) attributable to Mohawk Industries, Inc.	\$ 99,633	(45,045)	237,806	(124,494)

#### 9. Stock-based compensation

The Company recognizes compensation expense for all share-based payments granted based on the grant-date fair value estimated in accordance with the provisions of the FASB Accounting Standards Codification topic ( ASC ) 718-10. Compensation expense is recognized on a straight-line basis over the options or awards estimated lives for fixed awards with ratable vesting provisions.

Under the Company's 2007 Incentive Plan ( 2007 Plan ), which was approved by the Company's stockholders on May 16, 2007, the Company reserved up to a maximum of 3,200 shares of common stock for issuance upon the grant or exercise of stock options, restricted stock, restricted

## Edgar Filing: MOHAWK INDUSTRIES INC - Form 10-Q

stock units ( RSUs ) and other types of awards, to directors and key employees through 2017. Option awards are granted with an exercise price equal to the market price of the Company's common stock on the date of the grant and generally vest between three and five years with a 10-year contractual term. Restricted stock and RSUs are granted with a price equal to the market price of the Company's common stock on the date of the grant and generally vest between three and five years.

The Company granted 76 and 40 options to employees at a weighted-average grant-date fair value of \$25.39 and \$19.10 per share for the six months ended July 2, 2011 and July 3, 2010, respectively. The Company recognized stock-based compensation costs related to stock options of \$450 (\$285 net of taxes) and \$549 (\$348 net of taxes) for the three months ended July 2, 2011 and July 3, 2010, respectively, and \$1,009 (\$639 net of taxes) and \$1,324 (\$839 net of taxes) for the six months ended July 2, 2011 and July 3, 2010,

**Table of Contents**

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

respectively, which has been allocated to selling, general and administrative expenses. Pre-tax unrecognized compensation expense for stock options granted to employees and outside directors, net of estimated forfeitures, was \$2,835 as of July 2, 2011, and will be recognized as expense over a weighted-average period of approximately 1.8 years.

The fair value of the option award is estimated on the date of grant using the Black-Scholes-Merton valuation model. Expected volatility is based on the historical volatility of the Company's common stock. The Company uses historical data to estimate option exercise and forfeiture rates within the valuation model.

The Company granted 196 and 89 RSUs at a weighted-average grant-date fair value of \$57.35 and \$46.94 per unit for the six months ended July 2, 2011 and July 3, 2010, respectively. The Company recognized stock-based compensation costs related to the issuance of RSUs of \$1,708 (\$1,082 net of taxes) and \$1,024 (\$648 net of taxes) for the three months ended July 2, 2011 and July 3, 2010, respectively, and \$4,979 (\$3,154 net of taxes) and \$2,075 (\$1,315 net of taxes) for the six months ended July 2, 2011 and July 3, 2010, respectively, which has been allocated to selling, general and administrative expenses. Pre-tax unrecognized compensation expense for unvested RSUs granted to employees, net of estimated forfeitures, was \$14,596 as of July 2, 2011, and will be recognized as expense over a weighted-average period of approximately 3.8 years.

The Company did not grant any restricted stock awards for the six months ended July 2, 2011. Compensation expense for restricted stock awards for the six months ended July 2, 2011 and July 3, 2010, respectively, was not significant.

10. Earnings per share

Basic net earnings per share (EPS) is calculated using net earnings available to common stockholders divided by the weighted-average number of shares of common stock outstanding for the period. Diluted EPS is similar to basic EPS except that the weighted-average number of shares is increased to include the number of additional common shares that would have been outstanding if the potentially dilutive common shares had been issued.

Dilutive common stock options are included in the diluted EPS calculation using the treasury stock method. Common stock options and unvested restricted shares (units) that were not included in the diluted EPS computation because the price was greater than the average market price of the common shares for the three months ended July 2, 2011 and July 3, 2010 were 1,119 and 1,208, respectively. Common stock options and unvested restricted shares (units) that were not included in the diluted EPS computation because the price was greater than the average market price of the common shares for the six months ended July 2, 2011 and July 3, 2010 were 1,125 and 1,199, respectively.



**Table of Contents**

## MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

	Three Months Ended		Six Months Ended	
	July 2, 2011	July 3, 2010	July 2, 2011	July 3, 2010
Net earnings attributable to Mohawk Industries, Inc.	\$ 60,903	68,081	84,345	88,619
Accretion of redeemable noncontrolling interest (1)		(3,057)		(3,057)
Net earnings available to common stockholders	\$ 60,903	65,024	84,345	85,562
Weighted-average common shares outstanding-basic and diluted:				
Weighted-average common shares outstanding - basic	68,744	68,585	68,709	68,554
Add weighted-average dilutive potential common shares - options and RSU s to purchase common shares, net	237	204	233	206
Weighted-average common shares outstanding-diluted	68,981	68,789	68,942	68,760
Basic earnings per share attributable to Mohawk Industries, Inc. (2)	\$ 0.89	0.95	1.23	1.25
Diluted earnings per share attributable to Mohawk Industries, Inc. (2)	\$ 0.88	0.95	1.22	1.24

- (1) Amount represents the adjustment to fair value of a redeemable noncontrolling interest in a consolidated subsidiary
- (2) Basic EPS for the three and six months ended July 3, 2010, includes a decrease of approximately \$0.04 (from \$0.99 and \$1.29, respectively), and diluted EPS for the three and six months ended July 3, 2010, includes a decrease of approximately \$0.04 (from \$1.29) and \$0.05 (from \$1.29), respectively, related to the correction of an immaterial error for a change in fair value of a redeemable noncontrolling interest in a consolidated subsidiary of the Company. For more information on this matter, see notes 1(b) and 16 to the notes to the consolidated financial statements in the Company's 2010 Annual Report on Form 10-K.

**11. Segment reporting**

The Company has three reporting segments: the Mohawk segment, the Dal-Tile segment and the Unilin segment. The Mohawk segment designs, manufactures, sources, distributes and markets its floor covering product lines, which include carpets, ceramic tile, laminate, rugs, carpet pad, hardwood and resilient, primarily in North America through its network of regional distribution centers and satellite warehouses using Company-operated trucks, common carrier or rail transportation. The segment's product lines are sold through various selling channels, which include independent floor covering retailers, home centers, mass merchandisers, department stores, commercial dealers and commercial end users. The Dal-Tile segment designs, manufactures, sources, distributes and markets a broad line of ceramic tile, porcelain tile, natural stone and other products, primarily in North America through its network of regional distribution centers and Company-operated sales service centers using Company-operated trucks, common carriers or rail transportation. The segment's product lines are sold through Company-owned sales service centers, independent distributors, home center retailers, tile and flooring retailers and contractors. The Unilin segment designs, manufactures, sources, licenses, distributes and markets laminate, hardwood flooring, roofing systems, insulation panels and other wood products, primarily in North America and Europe through various selling channels, which include retailers, independent distributors and home centers.

The accounting policies for each operating segment are consistent with the Company's policies for the consolidated financial statements. Amounts disclosed for each segment are prior to any elimination or consolidation entries. Corporate general and administrative expenses attributable to each segment are estimated and allocated accordingly. Segment performance is evaluated based on operating income.



**Table of Contents**

## MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

Segment information is as follows:

	Three Months Ended		Six Months Ended	
	July 2, 2011	July 3, 2010	July 2, 2011	July 3, 2010
Net sales:				
Mohawk.	\$ 758,064	747,582	1,449,229	1,464,165
Dal-Tile	379,469	363,618	723,884	705,014
Unilin	363,097	308,385	688,929	614,265
Intersegment sales	(22,776)	(19,499)	(40,593)	(36,122)
	\$ 1,477,854	1,400,086	2,821,449	2,747,322
Operating income:				
Mohawk	\$ 31,201	26,345	48,241	42,973
Dal-Tile	32,138	28,124	49,838	43,519
Unilin	46,209	42,336	72,459	68,794
Corporate and eliminations	(7,848)	(7,079)	(12,754)	(11,939)
	\$ 101,700	89,726	157,784	143,347

  

	July 2, 2011	December 31, 2010
Assets:		
Mohawk	\$ 1,783,630	1,637,319
Dal-Tile	1,700,482	1,644,448
Unilin	2,717,032	2,475,049
Corporate and intersegment eliminations	187,856	342,110
	\$ 6,389,000	6,098,926

## 12. Commitments, contingencies and other

The Company is involved in litigation from time to time in the regular course of its business. Except as noted below, there are no material legal proceedings pending or known by the Company to be contemplated to which the Company is a party or to which any of its property is subject.

Beginning in August 2010, a series of civil lawsuits was initiated in several U.S. federal courts alleging that certain manufacturers of polyurethane foam products and competitors of the Company's carpet underlay division had engaged in price fixing in violation of U.S. antitrust laws. Mohawk has been named as a defendant in seven of the 43 cases filed (the first on August 26, 2010), as well as in two consolidated amended class action complaints, the first filed on February 28, 2011, on behalf of a class of all direct purchasers of polyurethane foam products, and the second filed on March 21, 2011, on behalf of a class of indirect purchasers. All pending cases in which the Company has been named as

## Edgar Filing: MOHAWK INDUSTRIES INC - Form 10-Q

a defendant have been filed in or transferred to the U.S. District Court for the Northern District of Ohio for consolidated pre-trial proceedings under the name *In re: Polyurethane Foam Antitrust Litigation*, Case No. 1:10-MDL-02196.

In these actions, the plaintiffs, on behalf of themselves and/or a class of purchasers, seek three times the amount of unspecified damages allegedly suffered as a result of alleged overcharges in the price of polyurethane foam products from at least 1999 to the present. Each plaintiff also seeks attorney fees, pre-judgment and post-judgment interest, court costs, and injunctive relief against future violations. In April 2011, the Company filed a motion to dismiss the class action claims brought by the direct purchasers, and in May 2011, the Company moved to dismiss the claims brought by the indirect purchasers. On July 19, 2011, the Court issued a written opinion denying all defendants' motions to dismiss. The Company denies all of the allegations in these actions and will vigorously defend itself.

The Company believes that adequate provisions for resolution of all contingencies, claims and pending litigation have been made for probable losses and that the ultimate outcome of these actions will not have a material adverse effect on its financial condition but could have a material adverse effect on its results of operations in a given quarter or year.

**Table of Contents**

## MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

The Company recorded pre-tax business restructuring charges of \$6,514 and \$13,327 for the three and six months ended July 2, 2011, respectively, of which \$5,532 and \$11,879 was recorded as cost of sales and \$982 and \$1,448 was recorded as selling, general and administrative expenses for the same periods, respectively. For the three and six months ended July 3, 2010, the Company recorded pre-tax business restructuring charges of \$4,929 and \$8,933, respectively, of which \$4,929 and \$8,786 was recorded as cost of sales and \$0 and \$147 was recorded as selling, general and administrative expenses for the same periods, respectively. The charges in 2011 and 2010 primarily relate to the Company's actions taken to lower its cost structure and improve the efficiency of its manufacturing and distribution operations as the Company adjusts to current economic conditions.

The restructuring activity for the first six months of 2011 is as follows:

	Asset write-downs	Lease impairments	Severance	Other restructuring costs	Total
Balance as of December 31, 2010	\$	10,983	2,107	420	13,510
Provisions:					
Mohawk segment	6,241	466	3,507	3,113	13,327
Dal-Tile segment					
Unilin segment					
Cash payments		(2,258)	(1,028)	(1,754)	(5,040)
Noncash items	(6,241)			(218)	(6,459)
Balance as of July 2, 2011	\$	9,191	4,586	1,561	15,338

The Company expects the remaining severance costs, lease impairments and other restructuring costs to be paid over the next five years.

**13. Debt**

On September 2, 2009, the Company entered into a \$600,000 four-year, senior, secured revolving credit facility (the "ABL Facility"). On July 8, 2011, subsequent to the balance sheet date, the Company entered into a \$900,000 five-year, senior, secured revolving credit facility (the "New Facility") and terminated the ABL Facility, which was originally set to mature on September 2, 2013. No early termination penalties were incurred as a result of the termination.

**ABL Facility**

The ABL Facility provided for a maximum of \$600,000 of revolving credit, subject to borrowing base availability, including limited amounts of credit in the form of letters of credit and swingline loans. The borrowing base was equal to specified percentages of eligible accounts receivable and inventories of the borrowers under the ABL Facility, which are subject to seasonal variations, less reserves established in good faith by the Administrative Agent under the ABL Facility. All obligations under the ABL Facility, and the guarantees of those obligations, were secured by a security interest in certain accounts receivable, inventories, certain deposit and securities accounts, tax refunds and other personal property (excluding intellectual property) directly relating to or arising from, and proceeds of, any of the foregoing.

## Edgar Filing: MOHAWK INDUSTRIES INC - Form 10-Q

At the Company's election, revolving loans under the ABL Facility bore interest at annual rates equal to either (a) LIBOR for 1-, 2-, 3- or 6-month periods, as selected by the Company, plus an applicable margin ranging between 2.75% and 3.25%, or (b) the higher of the prime rate, the Federal Funds rate plus 0.5%, or a one-month LIBOR rate, plus an applicable margin ranging between 1.25% and 1.75%. The Company also

**Table of Contents**

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

paid a commitment fee to the lenders under the ABL Facility on the average amount by which the aggregate commitments of the lenders exceeded utilization of the ABL Facility equal to 0.65% per annum during any quarter that this excess was 50% or more and 0.50% per annum during any quarter that this excess was less than 50%.

The ABL Facility included certain affirmative and negative covenants that imposed restrictions on the Company's financial and business operations, including limitations on debt, liens, investments, fundamental changes, asset dispositions, dividends and other similar restricted payments, transactions with affiliates, payments and modifications of certain existing debt, future negative pledges, and changes in the nature of the Company's business. The Company was also required to maintain a fixed charge coverage ratio of 1.1 to 1.0 during any period that the unutilized amount available under the ABL Facility was less than 15% of the lenders' aggregated commitments.

As of July 2, 2011, the amount utilized under the ABL Facility was \$360,100 resulting in a total of \$239,900 available under the ABL Facility. The amount utilized included \$253,000 of borrowings, \$53,542 of standby letters of credit guaranteeing the Company's industrial revenue bonds and \$53,558 of standby letters of credit related to various insurance contracts and foreign vendor commitments.

Senior Secured Credit Facility

The New Facility is scheduled to mature on July 8, 2016. The New Facility provides for a maximum of \$900,000 of revolving credit, including limited amounts of credit in the form of letters of credit and swingline loans. The Company can terminate and prepay the New Facility at any time without payment of any termination or prepayment penalty (other than customary breakage costs in respect of loans bearing interest at a rate based on LIBOR).

At the Company's election, revolving loans under the New Facility bear interest at annual rates equal to either (a) LIBOR for 1-, 2-, 3- or 6- month periods, as selected by the Company, plus an applicable margin ranging between 1.25% and 2.0%, or (b) the higher of the Bank of America, N.A. prime rate, the Federal Funds rate plus 0.5%, and a monthly LIBOR rate plus 1.0%, plus an applicable margin ranging between 0.25% and 1.0%. The Company also pays a commitment fee to the Lenders under the New Facility on the average amount by which the aggregate commitments of the Lenders exceed utilization of the New Facility ranging from 0.25% to 0.4% per annum. The applicable margin and the commitment fee are determined based on the Company's Consolidated Net Leverage Ratio (with applicable margins and the commitment fee increasing as the ratio increases).

All obligations of the Company and the other borrowers under the New Facility are required to be guaranteed by all of the Company's material domestic subsidiaries and all obligations of borrowers that are foreign subsidiaries are guaranteed by those foreign subsidiaries of the Company which the Company designates as guarantors. All obligations under the New Facility, and the guarantees of those obligations, are secured by a security interest in domestic accounts receivable and inventories, certain shares of capital stock (or equivalent ownership interests) of the domestic borrowers and domestic guarantors' subsidiaries, and proceeds of any of the foregoing. The amount of the obligations under the New Facility secured by such shares of capital stock and equivalent ownership interests is limited to the lesser of (i) the aggregate amount permitted to be secured under the Company's Indenture dated as of April 2, 2002 without requiring the notes issued under that Indenture to be secured equally and ratably by such shares of capital stock and equivalent ownership interests and (ii) the aggregate amount permitted to be secured under the Company's Indenture dated as of January 9, 2006 (as supplemented by that first supplemental indenture dated as of January 17, 2006) without requiring the notes issued under that Indenture to be secured equally and ratably by such shares of capital stock and equivalent ownership interests.

If at any time (a) either (i) the Company's corporate family rating or senior unsecured rating, whichever is in effect from Moody's Investors Service, Inc. (Moody's) is Baa3 or better (with a stable outlook or better)





## Table of Contents

### MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

#### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

and the Company's corporate rating from Standard & Poor's Financial Services LLC (S&P) is BB+ or better (with a stable outlook or better) or (ii) the Moody's rating is Ba1 or better (with a stable outlook or better) and the S&P rating is BBB- or better (with a stable outlook or better) and (b) no default or event of default has occurred and is continuing, then upon the Company's request, the foregoing security interests will be released. The Company is required to reinstate such security interests after release if: (a) both (i) the Moody's rating is Ba2 and (ii) the S&P rating is BB, (b) (i) the Moody's rating is Ba3 or lower and (ii) the S&P rating is below BBB- (with a stable outlook or better) or (c) (i) the Moody's rating is below Baa3 (with a stable outlook or better) and (ii) the S&P rating is BB- or lower.

The New Facility includes certain affirmative and negative covenants that impose restrictions on the Company's financial and business operations, including limitations on liens, indebtedness, investments, fundamental changes, asset dispositions, dividends and other similar restricted payments, transactions with affiliates, payments and modifications of certain existing debt, future negative pledges, and changes in the nature of the Company's business. Many of these limitations are subject to numerous exceptions. The Company is also required to maintain a Consolidated Interest Coverage Ratio of at least 3.0 to 1.0 and a Consolidated Net Leverage Ratio of no more than 3.75 to 1.0, each as of the last day of any fiscal quarter, as defined in the New Facility. The New Facility also contains customary representations and warranties and events of default, subject to customary grace periods.

As of July 8, 2011, the amount utilized under the New Facility was \$407,100 resulting in a total of \$492,900 available under the New Facility. The amount utilized included \$300,000 of borrowings, \$53,542 of standby letters of credit guaranteeing the Company's industrial revenue bonds and \$53,558 of standby letters of credit related to various insurance contracts and foreign vendor commitments.

#### Senior Notes

On January 17, 2006, the Company issued \$500,000 aggregate principal amount of 5.75% senior notes due January 15, 2011 and \$900,000 aggregate principal amount of 6.125% notes due January 15, 2016. Interest payable on these notes is subject to adjustment if either Moody's or S&P, or both, downgrades the rating assigned to the notes. Each rating agency downgrade results in a 0.25% increase in the interest rate, subject to a maximum increase of 1% per rating agency. If later the rating of these notes improves, then the interest rates would be reduced accordingly. Each 0.25% increase in the interest rate of these notes would increase the Company's interest expense by approximately \$63 per quarter per \$100,000 of outstanding notes. Interest rates have been increased by an aggregate amount of 0.75% as a result of downgrades by Moody's and S&P since 2008. Additional downgrades in the Company's credit ratings could further increase the cost of its existing credit and adversely affect the cost of and ability to obtain additional credit in the future. During the first quarter of 2011, the Company repaid the remaining outstanding \$298,248, 5.75% senior notes due January 15, 2011, at maturity with cash on hand and borrowings under the ABL Facility.

In 2002, the Company issued \$400,000 aggregate principal amount of its senior 7.20% notes due April 15, 2012.

#### 14. Fair value

ASC 825-10, formerly the FASB Staff Position FAS 107-1 and Accounting Principles Board 28-1, *Interim Disclosures About Fair Value of Financial Instruments*, requires disclosures about fair value of financial instruments in interim reporting periods of publicly-traded companies.

**Table of Contents**

## MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

The fair value and carrying value of our debt instruments are detailed as follows:

	July 2, 2011		December 31, 2010	
	Fair Value	Carrying Value	Fair Value	Carrying Value
5.75% notes, payable January 15, 2011 interest payable semiannually	\$		296,459	298,248
7.20% senior notes, payable April 15, 2012 interest payable semiannually	410,400	400,000	422,400	400,000
6.125% notes, payable January 15, 2016 interest payable semiannually	975,600	900,000	963,000	900,000
Four-year senior secured credit facility, due September 2, 2013	253,000	253,000		
Industrial revenue bonds, capital leases and other	55,335	55,335	55,334	55,334
Total long-term debt	1,694,335	1,608,335	1,737,193	1,653,582
Less current portion	463,585	453,185	348,799	350,588
Long-term debt, less current portion	\$ 1,230,750	1,155,150	1,388,394	1,302,994

The fair values of the Company's debt instruments were estimated using market observable inputs, including quoted prices in active markets, market indices and interest rate measurements. Within the hierarchy of fair value measurements, these are Level 2 fair values.

The carrying amounts of cash and cash equivalents, receivables, accounts payable and accrued expenses approximate their fair values because of the relatively short-term maturities of these instruments.

## **Table of Contents**

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

#### **Overview**

The Company is a leading producer of floor covering products for residential and commercial applications in the U.S. and residential applications in Europe with net sales in 2010 of \$5.3 billion. The Company is the second largest carpet and rug manufacturer and one of the largest manufacturers, marketers and distributors of ceramic tile, natural stone and hardwood flooring in the U.S., as well as a leading producer of laminate flooring in the U.S. and Europe. In 2010, the primary categories of the U.S. floor covering industry were carpet and rug (55%), resilient and rubber (13%), ceramic tile (12%), hardwood (9%), stone (6%) and laminate (5%).

The U.S. floor covering industry experienced declining demand beginning in the fourth quarter of 2006 that worsened during the latter parts of 2008, and continued to decline in 2009. In the first half of 2010 demand showed signs of recovering, but first half gains were lost in the second half of the year. Overall industry conditions in the U.S. are expected to improve during 2011, although the timing and size of a sustained recovery within the market remains uncertain.

The Company has three reporting segments: the Mohawk segment, the Dal-Tile segment and the Unilin segment. The Mohawk segment designs, manufactures, sources, distributes and markets its floor covering product lines, which include carpets, ceramic tile, laminate, rugs, carpet pad, hardwood and resilient, primarily in North America through its network of regional distribution centers and satellite warehouses using Company-operated trucks, common carrier or rail transportation. The segment's product lines are sold through various selling channels, which include independent floor covering retailers, home centers, mass merchandisers, department stores, commercial dealers and commercial end users. The Dal-Tile segment designs, manufactures, sources, distributes and markets a broad line of ceramic tile, porcelain tile, natural stone and other products, primarily in North America through its network of regional distribution centers and Company-operated sales service centers using Company-operated trucks, common carriers or rail transportation. The segment's product lines are sold through Company-owned sales service centers, independent distributors, home center retailers, tile and flooring retailers and contractors. The Unilin segment designs, manufactures, sources, licenses, distributes and markets laminate, hardwood flooring, roofing systems, insulation panels and other wood products, primarily in North America and Europe through various selling channels, which include retailers, independent distributors and home centers.

For the three months ended July 2, 2011, net earnings attributable to the Company were \$60.9 million, or diluted earnings per share (EPS) of \$0.88, compared to the net earnings attributable to the Company of \$68.1 million, or diluted EPS of \$0.95, for the three months ended July 3, 2010. For the six months ended July 2, 2011, net earnings attributable to the Company were \$84.3 million, or diluted EPS of \$1.22, compared to the net earnings attributable to the Company of \$88.6 million, or diluted EPS of \$1.24, for the six months ended July 3, 2010. The three and six months ended July 3, 2010 include a tax benefit of approximately \$30 million related to the settlement of certain tax contingencies and higher interest expense of \$7.5 million related to a premium paid to extinguish approximately \$200 million aggregate principal amount of senior notes. In addition to these 2010 impacts, the change in diluted EPS for the three and six months ended July 2, 2011, is primarily the result of the favorable net impact of price and product mix, lower selling, general and administrative costs, primarily as a result of the net benefits of restructuring actions taken in 2009 and 2010, and lower interest costs on outstanding debt, partially offset by higher inflationary costs, primarily related to raw materials.

## **Table of Contents**

### **Results of Operations**

#### **Quarter Ended July 2, 2011, as Compared with Quarter Ended July 3, 2010**

##### **Net sales**

Net sales for the three months ended July 2, 2011 were \$1,477.9 million, reflecting an increase of \$77.8 million, or 5.6%, from the \$1,400.1 million reported for the three months ended July 3, 2010. The increase was primarily due to the impact of favorable foreign exchange rates of approximately \$36 million, the net effect of price and product mix of approximately \$25 million and higher sales volume of approximately \$17 million.

*Mohawk Segment* - Net sales increased \$10.5 million, or 1.4%, to \$758.1 million for the three months ended July 2, 2011, compared to \$747.6 million for the three months ended July 3, 2010. The increase was primarily driven by the net effect of price and product mix of approximately \$7 million and higher sales volume of approximately \$4 million.

*Dal-Tile Segment* - Net sales increased \$15.9 million, or 4.4%, to \$379.5 million for the three months ended July 2, 2011, compared to \$363.6 million for the three months ended July 3, 2010. The increase was primarily driven by higher sales volume of approximately \$9 million, the net effect of price and product mix of approximately \$5 million and the impact of favorable foreign exchange rates of approximately \$2 million.

*Unilin Segment* - Net sales increased \$54.7 million, or 17.7%, to \$363.1 million for the three months ended July 2, 2011, compared to \$308.4 million for the three months ended July 3, 2010. The increase was due to favorable foreign exchange rates of approximately \$34 million, the net effect of price and product mix of approximately \$13 million and higher sales volume of approximately \$8 million.

##### **Gross profit**

Gross profit for the three months ended July 2, 2011 was \$382.2 million (25.9% of net sales) and increased by \$7.5 million or 2.0% compared to gross profit of \$374.8 million (26.8% of net sales) for the three months ended July 3, 2010. Gross profit was favorably impacted by the net effect of price and product mix of approximately \$25 million, lower manufacturing costs of approximately \$18 million as a result of cost savings initiatives implemented by the Company and various restructuring actions, including manufacturing facility consolidations, workforce reductions and productivity improvements, the impact of favorable foreign exchange rates of approximately \$10 million and higher sales volume of approximately \$1 million, partially offset by higher inflationary costs of approximately \$45 million, primarily related to raw materials and energy, and approximately \$1 million in higher restructuring charges. Gross profit as a percent of net sales was unfavorably impacted by higher inflationary costs.

##### **Selling, general and administrative expenses**

Selling, general and administrative expenses for the three months ended July 2, 2011 were \$280.5 million (19.0% of net sales), reflecting a decrease of \$4.5 million, or 1.6%, compared to \$285.0 million (20.4% of net sales) for the three months ended July 3, 2010. The decrease in selling, general and administrative expenses is primarily driven by the benefits of various restructuring actions and cost savings initiatives implemented by the Company, including facility consolidations and productivity improvements, partially offset by unfavorable foreign exchange rates.

##### **Operating income**

Operating income for the three months ended July 2, 2011 was \$101.7 million (6.9% of net sales) reflecting a \$12.0, million, or 13.3%, increase compared to an operating income of \$89.7 million (6.4% of net sales) for the three months ended July 3, 2010. Operating income was favorably impacted by lower manufacturing costs and selling, general and administrative expenses of approximately \$30 million, as a result of cost savings initiatives implemented by the Company and various restructuring actions, and the net effect of price and product mix of approximately \$25 million, partially offset by higher inflationary costs of approximately \$46 million, primarily related to raw materials and energy.

## **Table of Contents**

*Mohawk Segment* - Operating income was \$31.2 million (4.1% of segment net sales) for the three months ended July 2, 2011 reflecting an increase of \$4.9 million compared to operating income of \$26.3 million (3.5% of segment net sales) for the three months ended July 3, 2010. Operating income was favorably impacted by lower manufacturing costs and selling, general and administrative expenses of approximately \$26 million, as a result of cost savings initiatives implemented by the Company and various restructuring actions, and the net effect of price and product mix of approximately \$9 million, partially offset by higher inflationary costs of approximately \$29 million, primarily related to raw materials, and approximately \$2 million of higher restructuring charges.

*Dal-Tile Segment* - Operating income was \$32.1 million (8.5% of segment net sales) for the three months ended July 2, 2011 reflecting an increase of \$4.0 million compared to operating income of \$28.1 million (7.7% of segment net sales) for the three months ended July 3, 2010. Operating income was favorably impacted by lower manufacturing costs and selling, general and administrative expenses of approximately \$7 million, as a result of cost savings initiatives implemented by the Company and various restructuring actions, the net effect of price and product mix of approximately \$3 million and higher sales volume of approximately \$1 million, partially offset by higher inflationary costs of approximately \$6 million, primarily related to raw materials and energy, and unfavorable foreign exchange rates of approximately \$1 million.

*Unilin Segment* - Operating income was \$46.2 million (12.7% of segment net sales) for the three months ended July 2, 2011 reflecting an increase of \$3.9 million compared to operating income of \$42.3 million (13.7% of segment net sales) for the three months ended July 3, 2010. The increase was primarily driven by the net effect of price and product mix of approximately \$14 million and favorable foreign exchange rates of approximately \$5 million, offset by higher inflationary costs of approximately \$11 million, primarily related to raw materials and energy, higher selling, general and administrative expenses of approximately \$2 million and lower sales volume of approximately \$1 million.

### **Interest expense**

Interest expense for the three months ended July 2, 2011 was \$25.8 million compared to \$39.0 million in the three months ended July 3, 2010. The decrease in interest expense for 2011 was due to lower interest costs on the Company's outstanding debt and lower debt levels. In addition, the 2010 interest expense includes a \$7.5 million premium paid to extinguish approximately \$200 million aggregate principal amount of senior notes.

### **Income tax expense**

For the three months ended July 2, 2011, the Company recorded income tax expense of \$13.4 million on earnings before income taxes of \$75.5 million for an effective tax rate of 17.8%, as compared to an income tax benefit of \$18.8 million on earnings before income taxes of \$50.2 million for an effective tax rate of (37.5)% for the three months ended July 3, 2010. The difference in the effective tax rate for the comparative period is primarily due to the benefit from the settlement of certain tax contingencies of approximately \$30 million recorded during the second quarter of 2010 and the geographical dispersion of earnings and losses for the current period.

### **Six Months Ended July 2, 2011, as Compared with Six Months Ended July 3, 2010**

#### **Net sales**

Net sales for the six months ended July 2, 2011 were \$2,821.4 million, reflecting an increase of \$74.1 million, or 2.7%, from the \$2,747.3 million reported for the six months ended July 3, 2010. The increase was primarily due to the net effect of price and product mix of approximately \$48 million and the impact of favorable foreign exchange rates of approximately \$35 million, partially offset by lower sales volume of approximately \$9 million, primarily related to continued weakness in the U.S. residential market.

*Mohawk Segment* - Net sales decreased \$14.9 million, or 1.0%, to \$1,449.2 million for the six months ended July 2, 2011, compared to \$1,464.2 million for the six months ended July 3, 2010. The decrease was primarily driven by lower sales volume of approximately \$24 million, primarily related to continued weakness in the U.S. residential market, partially offset by the net effect of price and product mix of approximately \$9 million.

## **Table of Contents**

*Dal-Tile Segment* - Net sales increased \$18.9 million, or 2.7%, to \$723.9 million for the six months ended July 2, 2011, compared to \$705.0 million for the six months ended July 3, 2010. The increase was primarily driven by the net effect of price and product mix of approximately \$8 million, higher sales volume of approximately \$7 million and the impact of favorable foreign exchange rates of approximately \$4 million.

*Unilin Segment* - Net sales increased \$74.7 million, or 12.2%, to \$688.9 million for the six months ended July 2, 2011, compared to \$614.3 million for the six months ended July 3, 2010. The increase was due to the net effect of price and product mix of approximately \$31 million, the impact of favorable foreign exchange rates of approximately \$31 million and higher sales volume of approximately \$13 million.

### **Gross profit**

Gross profit for the six months ended July 2, 2011 was \$723.8 million (25.7% of net sales) and increased by \$7.8 million compared to gross profit of \$716.0 million (26.1% of net sales) for the six months ended July 3, 2010. Gross profit was favorably impacted by the net effect of price and product mix of approximately \$56 million, lower manufacturing costs of approximately \$38 million as a result of cost savings initiatives implemented by the Company and various restructuring actions, including manufacturing facility consolidations, workforce reductions and productivity improvements, and favorable foreign exchange rates of approximately \$9 million, offset by higher inflationary costs of approximately \$85 million, primarily related to raw materials and energy, lower sales volume of approximately \$7 million, primarily channel mix, and approximately \$3 million of higher restructuring charges.

### **Selling, general and administrative expenses**

Selling, general and administrative expenses for the six months ended July 2, 2011 were \$566.1 million (20.1% of net sales), reflecting a decrease of \$6.6 million, compared to \$572.7 million (20.8% of net sales) for the six months ended July 3, 2010. The decrease in selling, general and administrative expenses is primarily driven by the benefits of various restructuring actions and cost savings initiatives implemented by the Company, including facility consolidations and productivity improvements, partially offset by unfavorable foreign exchange rates.

### **Operating income**

Operating income for the six months ended July 2, 2011 was \$157.8 million (5.6% of net sales) reflecting a \$14.4 million increase compared to an operating income of \$143.3 million (5.2% of net sales) for the six months ended July 3, 2010. Operating income was favorably impacted by the net effect of price and product mix of approximately \$55 million, lower manufacturing costs and selling, general and administrative expenses of approximately \$53 million as a result of cost savings initiatives implemented by the Company and various restructuring actions, including manufacturing facility consolidations, workforce reductions and productivity improvements, and the impact of favorable foreign exchange rates of approximately \$3 million, partially offset by higher inflationary costs of approximately \$86 million, primarily related to raw materials and energy, lower sales volume of approximately \$7 million and higher restructuring charges of approximately \$4 million.

*Mohawk Segment* - Operating income was \$48.2 million (3.3% of segment net sales) for the six months ended July 2, 2011 reflecting an increase of \$5.3 million compared to operating income of \$43.0 million (2.9% of segment net sales) for the six months ended July 3, 2010. Operating income was favorably impacted by lower manufacturing costs and selling, general and administrative expenses of approximately \$47 million as a result of cost savings initiatives implemented by the Company and various restructuring actions, including manufacturing facility consolidations, workforce reductions and productivity improvements, and the net effect of price and product mix of approximately \$20 million, partially offset by higher inflationary costs of approximately \$47 million, primarily related to raw materials and energy, lower sales volume of approximately \$8 million and higher restructuring charges of approximately \$5 million.

*Dal-Tile Segment* - Operating income was \$49.8 million (6.9% of segment net sales) for the six months ended July 2, 2011 reflecting an increase of \$6.3 million compared to operating income of \$43.5 million (6.2%

## **Table of Contents**

of segment net sales) for the six months ended July 3, 2010. Operating income was favorably impacted by lower manufacturing costs, selling, general and administrative expenses and freight costs of approximately \$12 million as a result of cost savings initiatives implemented by the Company and various restructuring actions, including manufacturing facility consolidations, workforce reductions and productivity improvements, and the net effect of price and product mix of approximately \$5 million, partially offset by higher inflationary costs of approximately \$9 million, primarily related to raw materials and energy and the impact of unfavorable foreign exchange rates of approximately \$2 million.

*Unilin Segment* - Operating income was \$72.5 million (10.5% of segment net sales) for the six months ended July 2, 2011 reflecting an increase of \$3.7 million compared to operating income of \$68.8 million (11.2% of segment net sales) for the six months ended July 3, 2010. The increase was primarily driven by the net effect of price and product mix of approximately \$31 million, favorable foreign exchange rates of approximately \$5 million, higher sales volume of approximately \$2 million, lower restructuring costs of approximately \$1 million, partially offset by higher inflationary costs of approximately \$35 million, primarily related to raw materials and energy.

### **Interest expense**

Interest expense for the six months ended July 2, 2011 was \$52.4 million compared to \$72.9 million in the six months ended July 3, 2010. The decrease in interest expense resulted from lower interest costs on the Company's outstanding debt and lower debt levels. In addition, the 2010 interest expense includes a \$7.5 million premium paid to extinguish approximately \$200 million aggregate principal amount of senior notes.

### **Income tax expense**

For the six months ended July 2, 2011, the Company recorded an income tax expense of \$18.4 million on earnings before income taxes of \$105.0 million for an effective tax rate of 17.5%, as compared to a benefit of \$15.8 million on earnings before income taxes of \$74.4 million for an effective tax rate of (21.3)% for the six months ended July 3, 2010. The difference in the effective tax rate for the comparative period is primarily due to the benefit from the settlement of certain tax contingencies of approximately \$30 million recorded during the second quarter of 2010 and the geographical dispersion of earnings and losses for the current period.

### **Liquidity and Capital Resources**

The Company's primary capital requirements are for working capital, capital expenditures and acquisitions. The Company's capital needs are met primarily through a combination of internally generated funds, bank credit lines, term and senior notes and credit terms from suppliers.

Cash flows provided by operating activities for the first six months of 2011 were \$28.6 million compared to \$89.0 million in the first six months of 2010. The decrease in cash provided by operating activities for the first six months of 2011 as compared to 2010 is primarily attributable to the 2010 tax refunds, the timing of receipts and customer mix changes in receivables and timing of disbursements.

Net cash used in investing activities for the first six months of 2011 was \$112.5 million compared to \$47.1 million in the first six months of 2010. The increase in investing activities primarily relates to higher capital expenditures related to additional extrusion capacity and expanding the Company's international manufacturing capabilities. Capital spending during the remainder of 2011, excluding acquisitions, is expected to range from approximately \$160 million to \$180 million and is intended to be used primarily to purchase equipment, add geographic capacity and to streamline manufacturing capabilities.

Net cash used in financing activities for the first six months of 2011 was \$3.4 million compared to net cash used in financing activities of \$212.0 million in the first six months of 2010. The change in cash used in financing activities as compared to the first six months of 2010 is primarily attributable to lower debt repayments, net of borrowings and restricted cash, and the change in outstanding checks.

On September 2, 2009, the Company entered into a four-year, senior, secured revolving credit facility (the ABL Facility). The ABL Facility provided for a maximum of \$600.0 million of revolving credit, subject to borrowing base availability, including limited amounts of credit in the form of letters of credit and swingline loans.

## **Table of Contents**

As of July 2, 2011, the amount utilized under the ABL Facility was \$360.1 million resulting in a total of \$239.9 million available under the ABL Facility. The amount utilized included \$253.0 million of borrowings, \$53.5 million of standby letters of credit guaranteeing the Company's industrial revenue bonds and \$33.6 million of standby letters of credit related to various insurance contracts and foreign vendor commitments.

On July 8, 2011, the Company entered into a five-year, senior, secured revolving credit facility (the New Facility) and terminated the ABL Facility, which was originally set to mature on September 2, 2013. No early termination penalties were incurred as a result of the termination. The New Facility provides for a maximum of \$900 million of revolving credit, including limited amounts of credit in the form of letters of credit and swingline loans.

The New Facility is scheduled to mature on July 8, 2016. The Company can terminate and prepay the New Facility at any time without payment of any termination or prepayment penalty (other than customary breakage costs in respect of loans bearing interest at a rate based on LIBOR).

At the Company's election, revolving loans under the New Facility bear interest at annual rates equal to either (a) LIBOR for 1-, 2-, 3- or 6- month periods, as selected by the Company, plus an applicable margin ranging between 1.25% and 2.0%, or (b) the higher of the Bank of America, N.A. prime rate, the Federal Funds rate plus 0.5%, and a monthly LIBOR rate plus 1.0%, plus an applicable margin ranging between 0.25% and 1.0%. The Company also pays a commitment fee to the Lenders under the New Facility on the average amount by which the aggregate commitments of the Lenders exceeds utilization of the New Facility ranging from 0.25% to 0.4% per annum. The applicable margin and the commitment fee are determined based on the Company's Consolidated Net Leverage Ratio (with applicable margins and the commitment fee increasing as the ratio increases).

All obligations of the Company and the other borrowers under the New Facility are required to be guaranteed by all of the Company's material domestic subsidiaries and all obligations of borrowers that are foreign subsidiaries are guaranteed by those foreign subsidiaries of the Company which the Company designates as guarantors. All obligations under the New Facility, and the guarantees of those obligations, are secured by a security interest in domestic accounts receivable and inventories, certain shares of capital stock (or equivalent ownership interests) of the domestic borrowers and domestic guarantors' subsidiaries, and proceeds of any of the foregoing. The amount of the obligations under the New Facility secured by such shares of capital stock and equivalent ownership interests is limited to the lesser of (i) the aggregate amount permitted to be secured under the Company's Indenture dated as of April 2, 2002 without requiring the notes issued under that Indenture to be secured equally and ratably by such shares of capital stock and equivalent ownership interests and (ii) the aggregate amount permitted to be secured under the Company's Indenture dated as of January 9, 2006 (as supplemented by that first supplemental indenture dated as of January 17, 2006) without requiring the notes issued under that Indenture to be secured equally and ratably by such shares of capital stock and equivalent ownership interests.

If at any time (a) either (i) the Company's corporate family rating or senior unsecured rating, whichever is in effect from Moody's Investors Service, Inc. (Moody's) is Baa3 or better (with a stable outlook or better) and the Company's corporate rating from Standard & Poor's Financial Services LLC (S&P) is BB+ or better (with a stable outlook or better) or (ii) the Moody's rating is Ba1 or better (with a stable outlook or better) and the S&P rating is BBB- or better (with a stable outlook or better) and (b) no default or event of default has occurred and is continuing, then upon the Company's request, the foregoing security interests will be released. The Company is required to reinstate such security interests after release if: (a) both (i) the Moody's rating is Ba2 and (ii) the S&P rating is BB, (b) (i) the Moody's rating is Ba3 or lower and (ii) the S&P rating is below BBB- (with a stable outlook or better) or (c) (i) the Moody's rating is below Baa3 (with a stable outlook or better) and (ii) the S&P rating is BB- or lower.

The New Facility includes certain affirmative and negative covenants that impose restrictions on the Company's financial and business operations, including limitations on liens, indebtedness, investments,



## **Table of Contents**

fundamental changes, asset dispositions, dividends and other similar restricted payments, transactions with affiliates, payments and modifications of certain existing debt, future negative pledges, and changes in the nature of the Company's business. Many of these limitations are subject to numerous exceptions. The Company is also required to maintain a Consolidated Interest Coverage Ratio of at least 3.0 to 1.0 and a Consolidated Net Leverage Ratio of no more than 3.75 to 1.0, each as of the last day of any fiscal quarter, as defined in the New Facility. The New Facility also contains customary representations and warranties and events of default, subject to customary grace periods.

As of July 8, 2011, the amount utilized under the New Facility was \$407.1 million resulting in a total of \$492.9 million available under the New Facility. The amount utilized included \$300.0 million of borrowings, \$53.5 million of standby letters of credit guaranteeing the Company's industrial revenue bonds and \$53.6 million of standby letters of credit related to various insurance contracts and foreign vendor commitments.

On January 17, 2006, the Company issued \$500.0 million aggregate principal amount of 5.75% senior notes due January 15, 2011 and \$900.0 million aggregate principal amount of 6.125% notes due January 15, 2016. Interest payable on these notes is subject to adjustment if either Moody's or S&P, or both, downgrades the rating assigned to the notes. Each rating agency downgrade results in a 0.25% increase in the interest rate, subject to a maximum increase of 1% per rating agency. If later the rating of these notes improves, then the interest rates would be reduced accordingly. Each 0.25% increase in the interest rate of these notes would increase the Company's interest expense by approximately \$0.1 million per quarter per \$100.0 million of outstanding notes. Currently, the interest rates have been increased by an aggregate amount of 0.75% as a result of downgrades by Moody's and S&P since 2008. Additional downgrades in the Company's credit ratings could further increase the cost of its existing credit and adversely affect the cost of and ability to obtain additional credit in the future. During the first quarter of 2011, the Company repaid the remaining outstanding \$298.2 million, 5.75% senior notes due January 15, 2011, at maturity with cash on hand and borrowings under the ABL Facility.

In 2002, the Company issued \$400.0 million aggregate principal amount of its senior 7.20% notes due April 15, 2012. The Company believes it will have sufficient cash and cash equivalents and unutilized borrowing availability under the New Facility or through new public debt offerings to repay the senior notes when due. However, there can be no assurances that the Company will be able to complete new public debt offerings, if necessary, to repay the senior notes, prior to the April 15, 2012 maturity date.

As of July 2, 2011, the Company had invested cash of \$240.8 million in money market AAA rated cash investments of which \$233.3 million was in Europe. The Company believes that its cash and cash equivalents on hand, cash generated from operations and availability under its New Facility will be sufficient to meet its capital expenditure, working capital and debt servicing requirements over the next twelve months.

The Company may from time to time seek to retire its outstanding debt through cash purchases in the open market, privately negotiated transactions or otherwise. Such repurchases, if any, will depend on prevailing market conditions, the Company's liquidity requirements, contractual restrictions and other factors. The amount involved may be material.

### **Contractual Obligations**

There have been no significant changes to the Company's contractual obligations as disclosed in the Company's 2010 Annual Report filed on Form 10-K.

### **Critical Accounting Policies and Estimates**

There have been no significant changes to the Company's critical accounting policies and estimates during the period. The Company's critical accounting policies and estimates are described in its 2010 Annual Report filed on Form 10-K.

## **Table of Contents**

### **Recent Accounting Pronouncements**

In June 2011, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update ( ASU ) No. 2011-05, *Comprehensive Income (Topic 220) Presentation of Comprehensive Income* ( ASU 2011-05 ). This update requires that the components of net income, the components of other comprehensive income and the total of comprehensive income be presented as a single continuous financial statement or in two separate but consecutive statements. The option of presenting other comprehensive income in the statement of stockholders' equity is eliminated. This update also requires the presentation on the face of the financial statements of reclassification adjustments for items that are reclassified from other comprehensive income to net income in the statements where the components of net income and the components of other comprehensive income are presented. ASU 2011-05 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011.

### **Impact of Inflation**

Inflation affects the Company's manufacturing costs, distribution costs and operating expenses. The Company expects raw material prices, many of which are petroleum based, to continue to fluctuate based upon worldwide supply and demand of commodities utilized in the Company's production processes. In the past, the Company has generally been able to pass along these price increases to its customers and has been able to enhance productivity and develop new product innovations to help offset increases in costs resulting from inflation in its operations.

### **Seasonality**

The Company is a calendar year-end company. With respect to its Mohawk and Dal-Tile segments, its results of operations for the first quarter tend to be the weakest. The second, third and fourth quarters typically produce higher net sales and operating income in these segments. These results are primarily due to consumer residential spending patterns for floor covering, which historically have decreased during the first two months of each year following the holiday season. The Unilin segment second and fourth quarters typically produce higher net sales and earnings followed by a moderate first quarter and a weaker third quarter. The third quarter is traditionally the weakest due to the European holiday in late summer.

### **Forward-Looking Information**

Certain of the statements in this Form 10-Q, particularly those anticipating future performance, business prospects, growth and operating strategies, proposed acquisitions, and similar matters, and those that include the words believes, anticipates, forecast, estimates or similar expressions constitute 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. For those statements, Mohawk claims the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. There can be no assurance that the forward-looking statements will be accurate because they are based on many assumptions, which involve risks and uncertainties. The following important factors could cause future results to differ: changes in economic or industry conditions; competition; inflation in raw material prices and other input costs; energy costs and supply; timing and level of capital expenditures; timing and implementation of price increases for the Company's products; impairment charges; integration of acquisitions; international operations, introduction of new products; rationalization of operations; claims; litigation; and other risks identified in Mohawk's SEC reports and public announcements.

**Table of Contents**

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

There have been no significant changes to the Company's exposure to market risk as disclosed in the Company's 2010 Annual Report filed on Form 10-K.

**Item 4. Controls and Procedures**

Based on an evaluation of the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended), which have been designed to provide reasonable assurance that such controls and procedures will meet their objectives, as of the end of the period covered by this report, the Company's Chief Executive Officer and Chief Financial Officer have concluded that such controls and procedures were effective at a reasonable assurance level for the period covered by this report.

No change in the Company's internal control over financial reporting occurred during the period covered by this report that materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## Table of Contents

### **PART II. OTHER INFORMATION**

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

The Company is involved in litigation from time to time in the regular course of its business. Except as noted below, there are no material legal proceedings pending or known by the Company to be contemplated to which the Company is a party or to which any of its property is subject.

Beginning in August 2010, a series of civil lawsuits was initiated in several U.S. federal courts alleging that certain manufacturers of polyurethane foam products and competitors of the Company's carpet underlay division had engaged in price fixing in violation of U.S. antitrust laws. Mohawk has been named as a defendant in seven of the 43 cases filed (the first on August 26, 2010), as well as in two consolidated amended class action complaints, the first filed on February 28, 2011, on behalf of a class of all direct purchasers of polyurethane foam products, and the second filed on March 21, 2011, on behalf of a class of indirect purchasers. All pending cases in which the Company has been named as a defendant have been filed in or transferred to the U.S. District Court for the Northern District of Ohio for consolidated pre-trial proceedings under the name *In re: Polyurethane Foam Antitrust Litigation*, Case No. 1:10-MDL-02196.

In these actions, the plaintiffs, on behalf of themselves and/or a class of purchasers, seek three times the amount of unspecified damages allegedly suffered as a result of alleged overcharges in the price of polyurethane foam products from at least 1999 to the present. Each plaintiff also seeks attorney fees, pre-judgment and post-judgment interest, court costs, and injunctive relief against future violations. In April 2011, the Company filed a motion to dismiss the class action claims brought by the direct purchasers, and in May 2011, the Company moved to dismiss the claims brought by the indirect purchasers. On July 19, 2011, the Court issued a written opinion denying all defendants' motions to dismiss. The Company denies all of the allegations in these actions and will vigorously defend itself.

The Company believes that adequate provisions for resolution of all contingencies, claims and pending litigation have been made for probable losses and that the ultimate outcome of these actions will not have a material adverse effect on its financial condition but could have a material adverse effect on its results of operations in a given quarter or year.

#### **Item 1A. Risk Factors**

In addition to the other information provided in this Form 10-Q, the following risk factors should be considered when evaluating an investment in shares of Common Stock.

If any of the events described in these risks were to occur, it could have a material adverse effect on the Company's business, financial condition and results of operations.

*The floor covering industry is sensitive to changes in general economic conditions, such as consumer confidence and income, corporate and government spending, interest rate levels, availability of credit and demand for housing. The downturn in the U.S. and global economies beginning in 2006, along with the residential and commercial markets in such economies, negatively impacted the floor covering industry and the Company's business. While overall economic conditions and the housing and flooring industries have begun to show signs of recovering, this improvement may be temporary and economic conditions may deteriorate in the foreseeable future. Further, significant or prolonged declines in such economies or in spending for replacement floor covering products or new construction activity could have a material adverse effect on the Company's business.*

The floor covering industry in which the Company participates is highly dependent on general economic conditions, such as consumer confidence and income, corporate and government spending, interest rate levels, availability of credit and demand for housing. The Company derives a majority of its sales from the replacement segment of the market. Therefore, economic changes that result in a significant or prolonged decline in spending for remodeling and replacement activities could have a material adverse effect on the Company's business and results of operations.

## **Table of Contents**

The floor covering industry is highly dependent on residential and commercial construction activity, including new construction, which is cyclical in nature and currently in a downturn. The downturn in the U.S. and global economies, along with the housing markets in such economies, negatively impacted the floor covering industry and the Company's business. Although the impact of a decline in new construction activity is typically accompanied by an increase in remodeling and replacement activity, these activities have also lagged during the downturn. While overall economic conditions and the housing and flooring industries have begun to show signs of recovering, this improvement may be temporary and economic conditions may deteriorate in the foreseeable future. A significant or prolonged decline in residential or commercial construction activity could have a material adverse effect on the Company's business and results of operations.

***In periods of rising costs, the Company may be unable to pass raw materials, energy and fuel-related cost increases on to its customers, which could have a material adverse effect on the Company's profitability.***

The prices of raw materials and fuel-related costs could vary significantly with market conditions. Although the Company generally attempts to pass on increases in raw material, energy and fuel-related costs to its customers, the Company's ability to do so is dependent upon the rate and magnitude of any increase, competitive pressures and market conditions for the Company's products. There have been in the past, and may be in the future, periods of time during which increases in these costs cannot be recovered. During such periods of time, the Company's profitability may be materially adversely affected.

***Uncertainty in the credit market or downturns in the global economy and the Company's business could affect the Company's overall availability and cost of credit.***

Uncertainty in the credit markets could affect the overall availability and cost of credit. Despite recent improvement in overall economic conditions, the impact of the economic downturn on the Company's ability to obtain financing, including any financing necessary to refinance its existing senior unsecured notes, in the future, and the cost and terms of it, remains uncertain. These and other economic factors could have a material adverse effect on demand for the Company's products and on its financial condition and operating results. Further, these generally negative economic and business conditions may factor into the Company's periodic credit ratings assessment by either or both Moody's Investors Service, Inc. and Standard & Poor's Ratings Services. A rating agency's evaluation is based on a number of factors, which include scale and diversification, brand strength, profitability, leverage, liquidity and interest coverage. During 2009, the Company's senior unsecured notes were downgraded by the rating agencies, which increased the Company's interest expense by approximately \$0.2 million per quarter per \$100 million of outstanding notes and could adversely affect the cost of and ability to obtain additional credit in the future. Additional downgrades in the Company's credit ratings could further increase the cost of its existing credit and adversely affect the cost of and ability to obtain additional credit in the future, and the Company can provide no assurances that additional downgrades will not occur.

***The Company has a significant level of indebtedness that must be repaid or refinanced. In addition, if the Company were unable to meet certain covenants contained in the Senior Secured Credit Facility, it may be required to repay borrowings under the Senior Secured Credit Facility prior to their maturity and may lose access to the Senior Secured Credit Facility for additional borrowings that may be necessary to fund its operations.***

The Company's outstanding 7.20% senior notes in the aggregate amount of \$400.0 million are due April 15, 2012. On July 8, 2011, the Company entered into a \$900 million five-year, senior, secured revolving credit facility (the "New Facility"). The Company believes it will have sufficient cash and cash equivalents and unutilized borrowing availability under the New Facility or through new public debt offerings to repay the senior notes when due. However, there can be no assurances that the Company will be able to complete new public debt offerings, if necessary, to repay the senior notes, prior to the April 15, 2012 maturity date. As of July 8, 2011, the amount utilized under the New Facility was \$407.1 million resulting in a total of \$492.9 million available under the New Facility. The amount utilized included \$300.0 million of borrowings, \$53.5 million of standby letters of credit guaranteeing the Company's industrial revenue bonds and \$53.6 million of standby letters of credit related to various insurance contracts and foreign vendor commitments.

## **Table of Contents**

During the term of the New Facility, if the Company's cash flow is worse than expected, the Company may need to refinance all or a portion of its indebtedness through a public debt offering or a new bank facility and may not be able to do so on terms acceptable to it, or at all. If the Company is unable to access debt markets at competitive rates or in sufficient amounts due to credit rating downgrades, market volatility, market disruption, or other factors, it could materially adversely affect the Company's ability to repay its indebtedness and otherwise have a substantial adverse effect on the Company's financial condition and results of operations.

Additionally, the New Facility includes certain affirmative and negative covenants that impose restrictions on the Company's financial and business operations, including limitations on liens, indebtedness, investments, fundamental changes, asset dispositions, dividends and other similar restricted payments, transactions with affiliates, payments and modifications of certain existing debt, future negative pledges, and changes in the nature of the Company's business. Many of these limitations are subject to numerous exceptions. The Company is also required to maintain a Consolidated Interest Coverage Ratio of at least 3.0 to 1.0 and a Consolidated Net Leverage Ratio of no more than 3.75 to 1.0, each as of the last day of any fiscal quarter, as defined in the New Facility.

***The Company faces intense competition in the flooring industry, which could decrease demand for the Company's products or force it to lower prices, which could have a material adverse effect on the Company's profitability.***

The floor covering industry is highly competitive. The Company faces competition from a number of manufacturers and independent distributors. Some of the Company's competitors are larger and have greater resources and access to capital than the Company does. Maintaining the Company's competitive position may require substantial investments in the Company's product development efforts, manufacturing facilities, distribution network and sales and marketing activities. Competitive pressures may also result in decreased demand for the Company's products or force the Company to lower prices. Any of these factors or others may impact demand which could have a material adverse effect on the Company's business.

***The Company may be unable to obtain raw materials on a timely basis, which could have a material adverse effect on the Company's business.***

The principal raw materials used in the Company's manufacturing operations include nylon, polypropylene, triexta and polyester resins and fibers, which are used primarily in the Company's carpet and rugs business; clay, talc, nepheline syenite and glazes, including frit (ground glass), zircon and stains, which are used exclusively in the Company's ceramic tile business; wood, paper, and resins which are used primarily in the Company's laminate flooring business. For certain of such raw materials, the Company is dependent on one or a small number of suppliers. An adverse change in the Company's relationship with such a supplier, the financial condition of such a supplier or such supplier's ability to manufacture or deliver such raw materials to the Company could lead to an interruption of supply or require the Company to purchase more expensive alternatives. An extended interruption in the supply of these or other raw materials used in the Company's business or in the supply of suitable substitute materials would disrupt the Company's operations, which could have a material adverse effect on the Company's business.

***Fluctuations in currency exchange rates may impact the Company's financial condition and results of operations and may affect the comparability of results between the Company's financial periods.***

The results of the Company's foreign subsidiaries reported in the local currency are translated into U.S. dollars for balance sheet accounts using exchange rates in effect as of the balance sheet date and for the statement of operations accounts using, principally, the Company's average rates during the period. The exchange rates between some of these currencies and the U.S. dollar in recent years have fluctuated significantly and may continue to do so in the future. The Company may not be able to manage effectively the Company's currency translation risks and volatility in currency exchange rates may have a material adverse effect on the Company's consolidated financial statements and affect comparability of the Company's results between financial periods.

## **Table of Contents**

*The Company may experience certain risks associated with acquisitions, joint ventures and strategic investments.*

The Company has typically grown its business through acquisitions. Growth through acquisitions involves risks, many of which may continue to affect the Company after the acquisition. The Company cannot give assurance that an acquired company will achieve the levels of revenue, profitability and production that the Company expects. The combination of an acquired company's business with the Company's existing businesses involves risks. The Company cannot be assured that reported earnings will meet expectations because of goodwill and intangible asset impairment, increased interest costs and issuance of additional securities or incurrence of debt. The Company may also face challenges in consolidating functions, integrating the Company's organizations, procedures, operations and product lines in a timely and efficient manner and retaining key personnel. These challenges may result in:

maintaining executive offices in different locations;

manufacturing and selling different types of products through different distribution channels;

conducting business from various locations;

maintaining different operating systems and software on different computer hardware; and

providing different employment and compensation arrangements for employees.

The diversion of management attention and any difficulties encountered in the transition and integration process could have a material adverse effect on the Company's revenues, level of expenses and operating results.

Failure to successfully manage and integrate an acquisition with the Company's existing operations could lead to the potential loss of customers of the acquired business, the potential loss of employees who may be vital to the new operations, the potential loss of business opportunities or other adverse consequences that could affect the Company's financial condition and results of operations. Even if integration occurs successfully, failure of the acquisition to achieve levels of anticipated sales growth, profitability or productivity or otherwise perform as expected, may adversely impact the Company's financial condition and results of operations.

In addition, we have made certain investments, including through joint ventures, in which we have a minority equity interest and lack management and operational control. The controlling joint venture partner in a joint venture investment may have business interests, strategies or goals that are inconsistent with ours, and business decisions or other actions or omissions of the controlling joint venture partner or the joint venture company may result in harm to our reputation or adversely affect the value of our investment in the joint venture.

*A failure to identify suitable acquisition candidates or partners for strategic investments and to complete acquisitions could have a material adverse effect on the Company's business.*

As part of the Company's business strategy, the Company intends to continue to pursue a wide array of potential strategic transactions, including acquisitions of complementary businesses, as well as strategic investments and joint ventures. Although the Company regularly evaluates such opportunities, the Company may not be able successfully to identify suitable acquisition candidates or investment opportunities, to obtain sufficient financing on acceptable terms to fund such strategic transactions, to complete acquisitions and integrate acquired businesses with the Company's existing businesses, or to manage profitably acquired businesses or strategic investments.

*The Company has been, and in the future may be, subject to costs, liabilities and other obligations under existing or new laws and regulations, which could be significant.*

The Company and its customers and suppliers are subject to various federal, state and local laws, regulations and licensing requirements. The Company faces risks and uncertainties related to compliance with and enforcement of increasingly numerous and complex federal, state and local laws and regulations. In addition, new laws and regulations may be enacted in the U.S. or abroad that may require the Company to incur

## Edgar Filing: MOHAWK INDUSTRIES INC - Form 10-Q

additional personnel-related, environmental, or other costs on an ongoing basis, such as recently enacted healthcare legislation in the United States.



## **Table of Contents**

Further, the Company's operations are subject to various environmental, health and safety laws and regulations, including those governing air emissions, wastewater discharges, and the use, storage, treatment, recycling and disposal of materials and finished product. The applicable requirements under these laws are subject to amendment, to the imposition of new or additional requirements and to changing interpretations of agencies or courts. The Company could incur material expenditures to comply with new or existing regulations, including fines and penalties and increased costs of its operations. For example, enactment of climate control legislation or other regulatory initiatives by the U.S. Congress or various states, or the adoption of regulations by the EPA and analogous state or foreign governmental agencies that restrict emissions of greenhouse gases in areas in which the Company conducts business could have an adverse effect on its operations and demand for its products. The Company's manufacturing processes use a significant amount of energy, especially natural gas. Increased regulation of energy use to address the possible emission of greenhouse gases and climate change could materially increase the Company's manufacturing costs.

The nature of the Company's business and operations, including the potential discovery of presently unknown environmental conditions, exposes it to the risk of claims under environmental, health and safety laws and regulations. The Company could incur material costs or liabilities in connection with such claims.

***The Company's business operations could suffer significant losses from natural disasters, catastrophes, fire or other unexpected events.***

Many of the Company's business activities involve substantial investments in manufacturing facilities and many products are produced at a limited number of locations. These facilities could be materially damaged by natural disasters, such as floods, tornados, hurricanes and earthquakes, or by fire or other unexpected events. The Company could incur uninsured losses and liabilities arising from such events, including damage to its reputation, and/or suffer material losses in operational capacity, which could have a material adverse impact on its business, financial condition and results of operations.

***The Company may be exposed to litigation, claims and other legal proceedings in the ordinary course of business relating to its products, which could affect its results of operations and financial condition.***

In the ordinary course of business, the Company is subject to a variety of product-related claims, lawsuits and legal proceedings, including those relating to product liability, product warranty, product recall, personal injury, and other matters that are inherently subject to many uncertainties regarding the possibility of a loss to the Company. Such matters could have a material adverse effect on its business, results of operations and financial condition if the Company is unable to successfully defend against or resolve these matters or if its insurance coverage is insufficient to satisfy any judgments against the Company or settlements relating to these matters. Although the Company has product liability insurance, the policies may not provide coverage for certain claims against the Company or may not be sufficient to cover all possible liabilities. Further, the Company may not be able to maintain insurance at commercially acceptable premium levels. Moreover, adverse publicity arising from claims made against the Company, even if the claims were not successful, could adversely affect the Company's reputation or the reputation and sales of its products.

***The Company manufactures, sources and sells many products internationally and is exposed to risks associated with doing business globally.***

The Company's manufacturing facilities in Mexico and Europe represent a significant portion of the Company's capacity for ceramic tile and laminate flooring, respectively, and the Company's European operations represent a significant source of the Company's revenues and profits. The business, regulatory and political environments in these countries differ from those in the U.S. In addition, the Company increasingly sells products, operates plants and invests in companies in other parts of the world. The Company's international sales, operations and investments are subject to risks and uncertainties, including:

changes in foreign country regulatory requirements;

differing business practices associated with foreign operations;

## **Table of Contents**

various import/export restrictions and the availability of required import/export licenses;

imposition of foreign tariffs and other trade barriers;

political, legal and economic instability;

foreign currency exchange rate fluctuations;

changes in foreign country tax rules, regulations and other requirements, such as changes in tax rates and statutory and judicial interpretations in tax laws;

inflation;

differing labor laws and changes in those laws;

work stoppages and disruptions in the shipping of imported and exported products;

government price controls;

extended payment terms and the inability to collect accounts receivable; and

tax inefficiencies and currency exchange controls that may adversely impact its ability to repatriate cash from non-U.S. subsidiaries. The Company cannot assure investors that it will succeed in developing and implementing policies and strategies to counter the foregoing factors effectively in each location where the Company does business and therefore that the foregoing factors will not have a material adverse effect on the Company's operations or upon its financial condition and results of operations.

***If the Company is unable to protect its intellectual property rights, particularly with respect to the Company's patented laminate flooring technology and its registered trademarks, the Company's business and prospects could be harmed.***

The future success and competitive position of certain of the Company's businesses, particularly the Company's laminate flooring business, depend in part upon the Company's ability to obtain and maintain proprietary technology used in the Company's principal product families. The Company relies, in part, on the patent, trade secret and trademark laws of the U.S. and countries in Europe, as well as confidentiality agreements with some of the Company's employees, to protect that technology.

The Company has obtained a number of patents relating to the Company's products and associated methods and has filed applications for additional patents, including the UNICLIC® family of patents, which protects Unilin's interlocking laminate flooring panel technology. The Company cannot assure investors that any patents owned by or issued to it will provide the Company with competitive advantages, that third parties will not challenge these patents, or that the Company's pending patent applications will be approved. In addition, patent filings by third parties, whether made before or after the date of the Company's filings, could render the Company's intellectual property less valuable.

Furthermore, despite the Company's efforts, the Company may be unable to prevent competitors and/or third parties from using the Company's technology without the Company's authorization, independently developing technology that is similar to that of the Company or designing around the Company's patents. The use of the Company's technology or similar technology by others could reduce or eliminate any competitive

## Edgar Filing: MOHAWK INDUSTRIES INC - Form 10-Q

advantage the Company has developed, cause the Company to lose sales or otherwise harm the Company's business. In addition, if the Company does not obtain sufficient protection for the Company's intellectual property, the Company's competitiveness in the markets it serves could be significantly impaired, which would limit the Company's growth and future revenue.

The Company has obtained and applied for numerous U.S. and Foreign Service marks and trademark registrations and will continue to evaluate the registration of additional service marks and trademarks, as appropriate. The Company cannot guarantee that any of the Company's pending or future applications will be approved by the applicable governmental authorities. Moreover, even if such applications are approved, third parties may seek to oppose or otherwise challenge the registrations. A failure to obtain trademark registrations in the U.S. and in other countries could limit the Company's ability to protect the Company's trademarks and impede the Company's marketing efforts in those jurisdictions.

## **Table of Contents**

The Company generally requires third parties with access to the Company's trade secrets to agree to keep such information confidential. While such measures are intended to protect the Company's trade secrets, there can be no assurance that these agreements will not be breached, that the Company will have adequate remedies for any breach or that the Company's confidential and proprietary information and technology will not be independently developed by or become otherwise known to third parties. In any of these circumstances, the Company's competitiveness could be significantly impaired, which would limit the Company's growth and future revenue.

***Companies may claim that the Company infringed their intellectual property or proprietary rights, which could cause it to incur significant expenses or prevent it from selling the Company's products.***

In the past, companies have claimed that certain technologies incorporated in the Company's products infringe their patent rights. There can be no assurance that the Company will not receive notices in the future from parties asserting that the Company's products infringe, or may infringe, those parties' intellectual property rights. The Company cannot be certain that the Company's products do not and will not infringe issued patents or other intellectual property rights of others. Historically, patent applications in the U.S. and some foreign countries have not been publicly disclosed until the patent is issued (or, in some recent cases, until 18 months following submission), and the Company may not be aware of currently filed patent applications that relate to the Company's products or processes. If patents are later issued on these applications, the Company may be liable for infringement.

Furthermore, the Company may initiate claims or litigation against parties for infringement of the Company's proprietary rights or to establish the invalidity, noninfringement, or unenforceability of the proprietary rights of others. Likewise, the Company may have similar claims brought against it by competitors. Litigation, either as plaintiff or defendant, could result in significant expense to the Company and divert the efforts of the Company's technical and management personnel from operations, whether or not such litigation is resolved in the Company's favor. In the event of an adverse ruling in any such litigation, the Company might be required to pay substantial damages (including punitive damages and attorney's fees), discontinue the use and sale of infringing products, expend significant resources to develop non-infringing technology or obtain licenses to infringing technology. There can be no assurance that licenses to disputed technology or intellectual property rights would be available on reasonable commercial terms, if at all. In the event of a successful claim against the Company along with failure to develop or license a substitute technology, the Company's business, financial condition and results of operations would be materially and adversely affected.

***The Company is subject to changing regulation of corporate governance and public disclosure that have increased both costs and the risk of noncompliance.***

The Company's stock is publicly traded. As a result, the Company is subject to the rules and regulations of federal and state agencies and financial market exchange entities charged with the protection of investors and the oversight of companies whose securities are publicly traded. These entities, including the Public Company Accounting Oversight Board, the Securities and Exchange Commission and New York Stock Exchange, frequently issue new requirements and regulations. The Company's efforts to comply with the regulations and interpretations have resulted in, and are likely to continue to result in, increased general and administrative costs and diversion of management's time and attention from revenue generating activities to compliance activities.

***Declines in the Company's business conditions may result in an impairment of the Company's tangible and intangible assets which could result in a material non-cash charge.***

A decrease in the Company's market capitalization, including a short-term decline in stock price, or a negative long-term performance outlook, could result in an impairment of its tangible and intangible assets which results when the carrying value of the Company's assets exceed their fair value. In 2008, the Company's goodwill and other intangible assets suffered an impairment and additional impairment charges could occur in future periods.

**Table of Contents**

*The long-term performance of the Company's business relies on its ability to attract, develop and retain talented management.*

To be successful, the Company must attract, develop and retain highly qualified and talented personnel in management, sales, marketing, product design and innovation and operations, and as it considers entering new international markets, skilled personnel familiar with those markets. The Company competes with multinational firms for these employees and invests significant resources in recruiting, developing, motivating and retaining them. The failure to attract, develop, motivate and retain key employees could negatively affect the Company's competitive position and its operating results.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**  
**None.**

**Item 3. Defaults Upon Senior Securities**  
**None.**

**Item 4. (Removed and Reserved)**  
**None.**

**Item 5. Other Information**  
**None.**

**Item 6. Exhibits**

<b>No.</b>	<b>Description</b>
31.1	Certification Pursuant to Rule 13a-14(a).
31.2	Certification Pursuant to Rule 13a-14(a).
32.1	Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

**Table of Contents**

**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.

**MOHAWK INDUSTRIES, INC.**

(Registrant)

Dated: August 5, 2011

By: /s/ Jeffrey S. Lorberbaum  
JEFFREY S. LORBERBAUM  
Chairman and Chief Executive Officer  
(principal executive officer)

Dated: August 5, 2011

By: /s/ Frank H. Boykin  
FRANK H. BOYKIN  
Chief Financial Officer  
(principal financial officer)