CARPENTER TECHNOLOGY CORP
Form 10-Q
February 01, 2018
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended December 31, 2017

or

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

For the transition period from to

Commission File Number 1-5828

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

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

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

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

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

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

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

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

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

The number of shares outstanding of the issuer’s common stock as of January 25, 2018 was 46,916,395.

Table of Contents

CARPENTER TECHNOLOGY CORPORATION
FORM 10-Q
INDEX

		Page
PART I	FINANCIAL INFORMATION	
Item 1	Financial Statements	
	Consolidated Balance Sheets (unaudited) as of December 31, 2017 and June 30, 2017	3
	Consolidated Statements of Income (unaudited) for the Three Months and Six Months Ended December 31, 2017 and 2016	4
	Consolidated Statements of Comprehensive Income (unaudited) for the Three Months and Six Months Ended December 31, 2017 and 2016	5
	Consolidated Statements of Cash Flows (unaudited) for the Six Months Ended December 31, 2017 and 2016	6
	Consolidated Statements of Changes in Equity (unaudited) for the Six Months Ended December 31, 2017 and 2016	7
	Notes to the Consolidated Financial Statements (unaudited)	8
Item 2	Management's Discussion and Analysis of Financial Condition and Results of Operations	26
Item 3	Quantitative and Qualitative Disclosures About Market Risk	46
Item 4	Controls and Procedures	47
PART II	OTHER INFORMATION	
Item 1	Legal Proceedings	47
Item 1A	Risk Factors	47
Item 2	Unregistered Sales of Equity Securities and Use of Proceeds	47
Item 6	Exhibits	48
	Signature	49

Table of Contents

PART I - FINANCIAL INFORMATION
Item 1. Financial Statements

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

	December 31, 2017	June 30, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$ 20.7	$66.3
Accounts receivable, net	297.2	290.4
Inventories	771.8	690.4
Other current assets	69.8	46.5
Total current assets	1,159.5	1,093.6
Property, plant and equipment, net	1,298.7	1,316.8
Goodwill	263.4	263.4
Other intangibles, net	61.6	64.9
Deferred income taxes	4.1	7.6
Other assets	156.8	131.8
Total assets	$ 2,944.1	$2,878.1
LIABILITIES		
Current liabilities:		
Short-term credit agreement borrowings	$ 9.3	$—
Current portion of long-term debt	55.0	55.0
Accounts payable	205.1	201.1
Accrued liabilities	118.4	139.9
Total current liabilities	387.8	396.0
Long-term debt, net of current portion	548.3	550.0
Accrued pension liabilities	369.7	378.3
Accrued postretirement benefits	123.4	122.6
Deferred income taxes	128.1	184.8
Other liabilities	50.0	47.8
Total liabilities	1,607.3	1,679.5
Contingencies and commitments (see Note 8)		
STOCKHOLDERS' EQUITY		
Common stock — authorized 100,000,000 shares; issued 55,450,861 shares at December 31, 2017 and 55,349,658 shares at June 30, 2017; outstanding 46,894,896 shares at December 31, 2017 and 46,753,180 shares at June 30, 2017	277.3	276.7
Capital in excess of par value	294.4	284.8
Reinvested earnings	1,420.1	1,321.8
Common stock in treasury (8,555,965 shares and 8,596,478 shares at December 31, 2017 and June 30, 2017, respectively), at cost	(339.9)	(341.6)
Accumulated other comprehensive loss	(315.1)	(343.1)
Total stockholders' equity	1,336.8	1,198.6
Total liabilities and stockholders' equity	$ 2,944.1	$2,878.1

See accompanying notes to consolidated financial statements.

3

Table of Contents

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

	Three Months Ended December 31,		Six Months Ended December 31,	
	2017	2016	2017	2016
Net sales	$487.8	$427.4	$967.5	$816.3
Cost of sales	402.1	364.9	796.2	707.8
Gross profit	85.7	62.5	171.3	108.5
Selling, general and administrative expenses	44.9	47.1	88.8	91.7
Operating income	40.8	15.4	82.5	16.8
Interest expense	(7.3)	(7.4)	(14.5)	(14.8)
Other income, net	0.2	0.3	0.9	1.0
Income before income taxes	33.7	8.3	68.9	3.0
Income tax (benefit) expense	(58.4)	1.3	(46.6)	2.2
Net income	$92.1	$7.0	$115.5	$0.8
EARNINGS PER COMMON SHARE:				
Basic	$1.93	$0.15	$2.43	$0.01
Diluted	$1.92	$0.15	$2.41	$0.01
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING:				
Basic	47.2	47.0	47.1	47.0
Diluted	47.6	47.1	47.5	47.1
Cash dividends per common share	$0.18	$0.18	$0.36	$0.36

See accompanying notes to consolidated financial statements.

Table of Contents

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

	Three Months Ended December 31,		Six Months Ended December 31,	
	2017	2016	2017	2016
Net income	$92.1	$7.0	$115.5	$0.8
Other comprehensive income, net of tax				
Pension and postretirement benefits, net of tax of $(0.8), $(3.5), $(2.1) and $(14.0), respectively	2.5	5.7	4.6	23.1
Net gain on derivative instruments, net of tax of $(5.6), $(2.4), $(10.4) and $(8.8), respectively	15.0	3.8	23.1	14.6
Foreign currency translation	(1.5)	(4.0)	0.3	(4.7)
Other comprehensive income	16.0	5.5	28.0	33.0
Comprehensive income	$108.1	$12.5	$143.5	$33.8

See accompanying notes to consolidated financial statements.

Table of Contents

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

	Six Months Ended December 31,	
	2017	2016
OPERATING ACTIVITIES		
Net income	$115.5	$0.8
Adjustments to reconcile net income to net cash provided from (used for) operating activities:		
Depreciation and amortization	58.0	58.7
Deferred income taxes	(66.2)	39.1
Net pension expense	7.1	31.0
Share-based compensation expense	8.1	6.5
Loss on disposals of property and equipment	0.4	0.3
Changes in working capital and other:		
Accounts receivable	(3.8)	0.8
Inventories	(81.5)	(74.2)
Other current assets	(17.6)	(5.6)
Accounts payable	11.8	17.2
Accrued liabilities	(6.2)	4.0
Pension plan contributions	(4.9)	(100.0)
Other postretirement plan contributions	(1.8)	(1.8)
Other, net	(1.6)	(2.2)
Net cash provided from (used for) operating activities	17.3	(25.4)
INVESTING ACTIVITIES		
Purchases of property, equipment and software	(55.7)	(45.1)
Net cash used for investing activities	(55.7)	(45.1)
FINANCING ACTIVITIES		
Credit agreement borrowings	—	80.0
Credit agreement repayments	—	(55.0)
Net change in short-term credit agreement borrowings	9.3	—
Dividends paid	(17.2)	(17.0)
Tax benefits on share-based compensation	—	0.3
Proceeds from stock options exercised	3.5	1.8
Withholding tax payments on share-based compensation awards	(0.6)	(0.4)
Net cash (used for) provided from financing activities	(5.0)	9.7
Effect of exchange rate changes on cash and cash equivalents	(2.2)	1.3
DECREASE IN CASH AND CASH EQUIVALENTS	(45.6)	(59.5)
Cash and cash equivalents at beginning of period	66.3	82.0
Cash and cash equivalents at end of period	$20.7	$22.5
SUPPLEMENTAL CASH FLOW INFORMATION:		
Non-cash investing activities:		
Acquisition of property, equipment and software	$5.8	$6.0

See accompanying notes to consolidated financial statements.

Table of Contents

CARPENTER TECHNOLOGY CORPORATION
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
FOR THE SIX MONTHS ENDED DECEMBER 31, 2017 AND 2016
(Unaudited)
($ in millions, except per share data)

	Common Stock					
	Par Value of $5	Capital in Excess of Par Value	Reinvested Earnings	Common Stock in Treasury	Accumulated Other Comprehensive (Loss) Income	Total Equity
Balances at June 30, 2017	$276.7	$ 284.8	$ 1,321.8	$ (341.6)	$ (343.1)	$ 1,198.6
Net income			115.5			115.5
Pension and postretirement benefits gain, net of tax					4.6	4.6
Net gain on derivative instruments, net of tax					23.1	23.1
Foreign currency translation					0.3	0.3
Cash Dividends:						0
Common @ $0.36 per share			(17.2)			(17.2)
Share-based compensation plans		6.7		1.7		8.4
Stock options exercised	0.6	2.9				3.5
Balances at December 31, 2017	$277.3	$ 294.4	$ 1,420.1	$ (339.9)	$ (315.1)	$ 1,336.8

	Common Stock					
	Par Value of $5	Capital in Excess of Par Value	Reinvested Earnings	Common Stock in Treasury	Accumulated Other Comprehensive (Loss) Income	Total Equity
Balances at June 30, 2016	$276.3	$ 273.5	$ 1,308.9	$ (343.9)	$ (409.9)	$ 1,104.9
Net income			0.8			0.8
Pension and postretirement benefits gain, net of tax					23.1	23.1
Net gain on derivative instruments, net of tax					14.6	14.6
Foreign currency translation					(4.7)	(4.7)
Cash Dividends:						0
Common @ $0.36 per share			(17.0)			(17.0)
Share-based compensation plans		5.0		1.5		6.5
Stock options exercised	0.4	1.4				1.8
Tax windfall on share-based compensation		0.3				0.3
Balances at December 31, 2016	$276.7	$ 280.2	$ 1,292.7	$ (342.4)	$ (376.9)	$ 1,130.3

See accompanying notes to consolidated financial statements.

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

1. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments, consisting of normal and recurring adjustments, considered necessary for a fair statement of the results are reflected in the interim periods presented. The June 30, 2017 consolidated balance sheet data was derived from audited financial statements, but does not include all of the disclosures required by accounting principles generally accepted in the United States of America. These unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and footnotes thereto included in Carpenter's annual report on Form 10-K for the fiscal year ended June 30, 2017 (the "2017 Form 10-K"). Operating results for the three and six months ended December 31, 2017 are not necessarily indicative of the operating results for any future period.

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

During the six months ended December 31, 2017, the Company changed the presentation of borrowings and repayments made under its revolving credit facility in the consolidated statements of cash flows. Prior year amounts have been reclassified to conform to the six months ended December 31, 2017 presentation.

2. Acquisition and Divestiture

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

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

3. Earnings per Common Share

The Company calculates basic and diluted earnings per share using the two class method. Under the two class method, earnings are allocated to common stock and participating securities (non-vested restricted shares and units that receive non-forfeitable dividends) according to their participation rights in dividends and undistributed earnings. The earnings available to each class of stock are divided by the weighted average number of outstanding shares for the period in each class. Diluted earnings per share assumes the issuance of common stock for all potentially dilutive share equivalents outstanding.

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

The calculations of basic and diluted earnings per common share for the three and six months ended December 31, 2017 and 2016 were as follows:

	Three Months Ended December 31,		Six Months Ended December 31,	
(in millions, except per share data)	2017	2016	2017	2016
Net income	$92.1	$7.0	$115.5	$0.8
Less: earnings and dividends allocated to participating securities	(0.9)	(0.1)	(1.0)	(0.1)
Earnings available for common stockholders used in calculation of basic earnings per common share	$91.2	$6.9	$114.5	$0.7
Weighted average number of common shares outstanding, basic	47.2	47.0	47.1	47.0
Basic earnings per common share	$1.93	$0.15	$2.43	$0.01
Net income	$92.1	$7.0	$115.5	$0.8
Less: earnings and dividends allocated to participating securities	(0.9)	(0.1)	(1.0)	(0.1)
Earnings available for common stockholders used in calculation of diluted earnings per common share	$91.2	$6.9	$114.5	$0.7
Weighted average number of common shares outstanding, basic	47.2	47.0	47.1	47.0
Effect of shares issuable under share-based compensation plans	0.4	0.1	0.4	0.1
Weighted average number of common shares outstanding, diluted	47.6	47.1	47.5	47.1
Diluted earnings per common share	$1.92	$0.15	$2.41	$0.01

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

	Three Months Ended December 31,		Six Months Ended December 31,	
(in millions)	2017	2016	2017	2016
Stock options	0.6	2.0	0.8	1.8

4. Inventories

Inventories consisted of the following components as of December 31, 2017 and June 30, 2017:

($ in millions)	December 31, 2017	June 30, 2017
Raw materials and supplies	$ 186.1	$ 152.8
Work in process	395.5	365.6
Finished and purchased products	190.2	172.0
Total inventory	$ 771.8	$ 690.4

Inventories are valued at the lower of cost or market. Cost for inventories is principally determined using the last-in, first-out (“LIFO”) inventory costing method. The Company also uses the first-in, first-out (“FIFO”) and average cost methods. As of December 31, 2017 and June 30, 2017, $128.8 million and $107.3 million of inventory, respectively, was accounted for using a method other than the LIFO inventory costing method.

5. Accrued Liabilities

Accrued liabilities consisted of the following as of December 31, 2017 and June 30, 2017:

($ in millions)	December 31, 2017	June 30, 2017
Accrued compensation and benefits	$ 52.6	$ 59.1
Accrued postretirement benefits	15.5	15.5
Accrued interest expense	11.2	11.2
Deferred revenue	10.7	9.8
Derivative financial instruments	2.9	13.1
Other	25.5	31.2
Total accrued liabilities	$ 118.4	$ 139.9

Table of Contents

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

6. Pension and Other Postretirement Benefits

The components of the net periodic benefit cost related to the Company's pension and other postretirement benefits for the three and six months ended December 31, 2017 and 2016 were as follows:

Three months ended December 31,	Pension Plans		Other Postretirement Plans	
($ in millions)	2017	2016	2017	2016
Service cost	$2.4	$7.7	$0.7	$0.9
Interest cost	13.0	12.4	2.4	2.3
Expected return on plan assets	(16.5)	(16.6)	(1.7)	(1.7)
Amortization of net loss	3.4	9.5	0.7	0.8
Amortization of prior service cost (benefit)	0.5	0.5	(1.3)	(1.6)
Net periodic benefit costs	$2.8	$13.5	$0.8	$0.7

Six months ended December 31,	Pension Plans		Other Postretirement Plans	
($ in millions)	2017	2016	2017	2016
Service cost	$4.7	$16.0	$1.3	$1.8
Interest cost	26.1	25.3	4.8	4.6
Expected return on plan assets	(33.0)	(31.9)	(3.5)	(3.4)
Amortization of net loss	6.8	18.9	1.5	1.6
Amortization of prior service cost (benefit)	1.0	0.8	(2.6)	(3.2)
Curtailment charge	—	0.5	—	—
Net periodic benefit costs	$5.6	$29.6	$1.5	$1.4

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

During the six months ended December 31, 2017 and 2016, the Company made $4.9 million and $100.0 million, respectively, of contributions to its qualified defined benefit pension plans. The Company currently expects to contribute $1.8 million to its qualified defined benefit pension plans during the remainder of fiscal year 2018.

7. Debt

On March 31, 2017, the Company entered into a $400.0 million unsecured revolving credit facility ("Credit Agreement") that extends to March 2022. Interest on the borrowings under the Credit Agreement accrue at variable rates, based upon LIBOR or a defined "Base Rate," both are determined based upon the rating of the Company's senior unsecured long-term debt (the "Debt Rating"). The applicable margin to be added to LIBOR ranges from 1.00% to 1.75% (1.50% as of December 31, 2017), and for Base Rate-determined loans, from 0.00% to 0.75% (0.50% as of December 31, 2017). The Company also pays a quarterly commitment fee ranging from 0.125% to 0.400% (0.275% as of December 31, 2017), determined based upon the Debt Rating, of the unused portion of the $400.0 million

commitment under the Credit Agreement. In addition, the Company must pay certain letter of credit fees, ranging from 1.00% to 1.75% (1.50% as of December 31, 2017), with respect to letters of credit issued under the Credit Agreement. The Company has the right to voluntarily prepay and re-borrow loans and to terminate or reduce the commitments under the facility. As of December 31, 2017, the Company had $6.0 million of issued letters of credit and $9.3 million of borrowings under the Credit Agreement with the balance of $384.7 million available to the Company.

The Company is subject to certain financial and restrictive covenants under the Credit Agreement, which, among other things, require the maintenance of a minimum interest coverage ratio of 3.50 to 1.00. The interest coverage ratio is defined in the Credit Agreement as, for any period, the ratio of consolidated earnings before interest, taxes, depreciation and amortization and non-cash net pension expense (“EBITDA”) to consolidated interest expense for such period. The Credit Agreement also requires the Company to maintain a debt to capital ratio of less than 55 percent. The debt to capital ratio is defined in the Credit Agreement as the ratio of consolidated indebtedness, as defined therein, to consolidated capitalization, as defined therein. As of December 31, 2017 and June 30, 2017, the Company was in compliance with all of the covenants of the Credit Agreement.

Long-term debt outstanding as of December 31, 2017 and June 30, 2017 consisted of the following:

($ in millions)	December 31, 2017	June 30, 2017
Medium-term notes, Series B at 6.97% to 7.10% due from April 2018 to May 2018 (face value of $55.0 million at December 31, 2017 and June 30, 2017)	$ 55.0	$ 55.0
Senior unsecured notes, 5.20% due July 2021 (face value of $250.0 million at December 31, 2017 and June 30, 2017)	249.3	251.2
Senior unsecured notes, 4.45% due March 2023 (face value of $300.0 million at December 31, 2017 and June 30, 2017)	299.0	298.8
Total	603.3	605.0
Less: amounts due within one year	55.0	55.0
Long-term debt, net of current portion	$ 548.3	$ 550.0

For the three months ended December 31, 2017 and 2016, interest costs totaled $7.9 million and $7.7 million, respectively, of which $0.6 million and $0.3 million, respectively, were capitalized as part of the cost of property, equipment and software. For the six months ended December 31, 2017 and 2016, interest costs totaled $15.6 million and $15.3 million, respectively, of which $1.1 million and $0.5 million, respectively, were capitalized as part of the cost of property, equipment and software.

8. Contingencies and Commitments

Environmental

The Company is subject to various federal, state, local and international environmental laws and regulations relating to pollution, protection of public health and the environment, natural resource damages and occupational safety and health. Although compliance with these laws and regulations may affect the costs of the Company’s operations, compliance costs to date have not been material. The Company has environmental remediation liabilities at some of its owned operating facilities and has been designated as a potentially responsible party (“PRP”) with respect to certain third party Superfund waste-disposal sites and other third party-owned sites. The Company accrues amounts for environmental remediation costs that represent management’s best estimate of the probable and reasonably estimable future costs related to environmental remediation. During the six months ended December 31, 2017, the Company increased the liability for a Company-owned former operating site by $0.1 million. The liabilities recorded for environmental remediation costs at Superfund sites, other third party-owned sites and Carpenter-owned current or former operating facilities remaining at December 31, 2017 and June 30, 2017 were $16.2 million and $16.1 million, respectively. Additionally, the Company has been notified that it may be a PRP with respect to other Superfund sites

as to which no proceedings have been instituted against the Company. Neither the exact amount of remediation costs nor the final method of their allocation among all designated PRPs at these Superfund sites have been determined. Accordingly, at this time, the Company cannot reasonably estimate expected costs for such matters. The liability for future environmental remediation costs that can be reasonably estimated is evaluated by management on a quarterly basis.

Other

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

9. Fair Value Measurements

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

Table of Contents

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

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

December 31, 2017	Fair Value Measurements Using Input Type
($ in millions)	Level 2
Assets:	
Marketable securities:	
Municipal auction rate securities	$ 3.5
Derivative financial instruments	31.7
Total assets	$ 35.2
Liabilities:	
Derivative financial instruments	$ 4.1

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

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

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

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

	December 31, 2017	June 30, 2017

($ in millions)	Carrying Value	Fair Value	Carrying Value	Fair Value
Long-term debt, including current portion	$603.3	$622.0	$605.0	$622.5
Company-owned life insurance	$16.0	$16.0	$15.9	$15.9

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

The fair values of long-term debt as of December 31, 2017 and June 30, 2017 were determined by using current interest rates for debt with terms and maturities similar to the Company's existing debt arrangements and accordingly would be classified as Level 2 inputs in the fair value hierarchy.

10. Derivatives and Hedging Activities

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

Cash Flow Hedging — Commodity forward contracts: The Company enters into commodity forward contracts to fix the price of a portion of anticipated future purchases of certain critical raw materials and energy to manage the risk of cash flow variability associated with volatile commodity prices. The commodity forward contracts have been designated as cash flow hedges. The qualifying hedge contracts are marked-to-market at each reporting date and any unrealized gains or losses are included in accumulated other comprehensive income (loss) ("AOCI") to the extent effective, and reclassified to cost of sales in the period during which the hedged transaction affects earnings or it becomes probable that the forecasted transaction will not occur. As of December 31, 2017, the Company had forward contracts to purchase 21.0 million pounds of certain raw materials with settlement dates through December 2023.

Cash Flow Hedging — Forward interest rate swaps: Historically, the Company has entered into forward interest rate swap contracts to manage the risk of cash flow variability associated with fixed interest debt expected to be issued. The forward interest rate swaps were designated as cash flow hedges. The qualifying hedge contracts were marked-to-market at each reporting date and any unrealized gains or losses were included in AOCI to the extent effective, and reclassified to interest expense in the period during which the hedged transaction affected earnings or it became probable that the forecasted transaction would not occur. Upon the issuance of the fixed rate debt, the forward interest rate swap contracts were terminated. The realized gains at the time the interest rate swap contracts were terminated are being amortized over the term of the underlying debt. For the three months ended December 31, 2017 and 2016, net gains of $0.1 million and $0.1 million, respectively, related to the previously terminated contracts were recorded as a reduction to interest expense. For the six months ended December 31, 2017 and 2016, net gains of $0.2 million and $0.2 million, respectively, related to the previously terminated contracts were recorded as a reduction to interest expense.

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

The Company also uses foreign currency forward contracts to protect certain short-term asset positions denominated in foreign currencies against the effect of changes in exchange rates. These positions do not qualify for hedge accounting and accordingly are marked-to-market at each reporting date through charges to other income and expense. As of December 31, 2017 and June 30, 2017, the fair value of the outstanding foreign currency forwards not designated as hedging instruments and the charges to income for changes in fair value for these contracts were not material.

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

Fair Value Hedging - Interest rate swaps: The Company uses interest rate swaps to achieve a level of floating rate debt relative to fixed rate debt where appropriate. The Company has designated fixed to floating interest rate swaps as fair value hedges. Accordingly, the changes in the fair value of these instruments are immediately recorded in earnings. The mark-to-market values of both the fair value hedging instruments and the underlying debt obligations are recorded as equal and offsetting gains and losses in interest expense in the consolidated statements of income. As of December 31, 2017 and June 30, 2017, the total notional amount of floating interest rate contracts was $150.0 million. For the three months ended December 31, 2017 and 2016, net gains of $0.2 million and $0.5 million, respectively, were recorded as a reduction to interest expense. For the six months ended December 31, 2017 and 2016, net gains of $0.4 million and $0.9 million, respectively, were recorded as a reduction to interest expense.

The fair value and location of outstanding derivative contracts recorded in the accompanying consolidated balance sheets were as follows as of December 31, 2017 and June 30, 2017:

December 31, 2017 ($ in millions)	Interest Rate Swaps	Foreign Currency Contracts	Commodity Contracts	Total Derivatives
Asset Derivatives:				
Derivatives designated as hedging instruments:				
Other current assets	$ 0.5	$ —	$ 12.7	$ 13.2
Other assets	0.6	—	17.9	18.5
Total asset derivatives	$ 1.1	$ —	$ 30.6	$ 31.7
Liability Derivatives:				
Derivatives designated as hedging instruments:				
Accrued liabilities	$ —	$ 1.3	$ 1.6	$ 2.9
Other liabilities	0.9	—	0.3	1.2
Total liability derivatives	$ 0.9	$ 1.3	$ 1.9	$ 4.1

June 30, 2017 ($ in millions)	Interest Rate Swaps	Foreign Currency Contracts	Commodity Contracts	Total Derivatives
Asset Derivatives:				
Derivatives designated as hedging instruments:				
Other current assets	$ 0.6	$ 0.2	$ 6.4	$ 7.2
Other assets	1.6	—	5.7	7.3
Total asset derivatives	$ 2.2	$ 0.2	$ 12.1	$ 14.5
Liability Derivatives:				
Derivatives designated as hedging instruments:				
Accrued liabilities	$ —	$ 1.0	$ 12.1	$ 13.1
Other liabilities	—	—	6.0	6.0
Total liability derivatives	$ —	$ 1.0	$ 18.1	$ 19.1

Substantially all of the derivative contracts are subject to master netting arrangements, or similar agreements with each counterparty, which provide for the option to settle contracts on a net basis when they settle on the same day and in the same currency. In addition, these arrangements provide for a net settlement of all contracts with a given counterparty in the event that the arrangement is terminated due to the occurrence of default or a termination event.

The Company presents the outstanding derivative contracts on a net basis by counterparty in the consolidated balance sheets. If the Company had chosen to present the derivative contracts on a gross basis, the total asset derivatives would have been $33.6 million and total liability derivatives would have been $6.0 million as of December 31, 2017.

According to the provisions of the Company's derivative arrangements, in the event that the fair value of outstanding derivative positions with certain counterparties exceeds certain thresholds, the Company may be required to issue cash collateral to the counterparties. As of December 31, 2017 and June 30, 2017, the Company had no cash collateral held by counterparties.

The Company is exposed to credit loss in the event of nonperformance by counterparties on its derivative instruments as well as credit or performance risk with respect to its customer commitments to perform. Although nonperformance is possible, the Company does not anticipate nonperformance by any of the parties. In addition, various master netting arrangements are in place with counterparties to facilitate settlements of gains and losses on these contracts.

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

Cash Flow Hedges

For derivative instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative is reported as a component of AOCI and reclassified into earnings in the same period or periods during which the hedged transactions affect earnings or it becomes probable the forecasted transactions will not occur. The following is a summary of the gains (losses) related to cash flow hedges recognized during the three and six months ended December 31, 2017 and 2016:

($ in millions)	Amount of Gain (Loss) Recognized in AOCI on Derivatives (Effective Portion) Three Months Ended December 31, 2017	2016	Six Months Ended December 31, 2017	2016
Derivatives in Cash Flow Hedging Relationship:				
Commodity contracts	$20.7	$(22.5)	$30.3	$(15.4)
Foreign exchange contracts	(0.3)	0.6	(0.7)	0.6
Total	$20.4	$(21.9)	$29.6	$(14.8)

($ in millions)	Location of (Loss) Gain Reclassified from AOCI into Income	Amount of (Loss) Gain Reclassified from AOCI into Income (Effective Portion) Three Months Ended December 31, 2017	2016	Amount of (Loss) Gain Reclassified from AOCI into Income (Ineffective Portion) Three Months Ended December 31, 2017	2016
Derivatives in Cash Flow Hedging Relationship:					
Commodity contracts	Cost of sales	$ (0.2)	$ (7.9)	$ —	$ —
Foreign exchange contracts	Net sales	(0.1)	0.5	—	—
Forward interest rate swaps	Interest expense	0.1	0.1	—	—
Total		$ (0.2)	$ (7.3)	$ —	$ —

($ in millions)	Location of (Loss) Gain Reclassified from AOCI into Income	Amount of (Loss) Gain Reclassified from AOCI into Income (Effective Portion) Six Months Ended December 31, 2017	2016	Amount of (Loss) Gain Reclassified from AOCI into Income (Ineffective Portion) Six Months Ended December 31, 2017	2016

Derivatives in Cash Flow Hedging Relationship:					
Commodity contracts	Cost of sales	$ (2.8)	$ (18.0)	$ (0.8)	$ 0.5
Foreign exchange contracts	Net sales	(0.5)	0.6	—	—
Forward interest rate swaps	Interest expense	0.2	0.2	—	—
Total		$ (3.1)	$ (17.2)	$ (0.8)	$ 0.5

The Company estimates that $10.5 million of net derivative gains included in AOCI as of December 31, 2017 will be reclassified into income within the next 12 months. No significant cash flow hedges were discontinued during the three and six months ended December 31, 2017.

11. Other Income, Net

Other income, net consisted of the following:

($ in millions)	Three Months Ended December 31,		Six Months Ended December 31,	
	2017	2016	2017	2016
Foreign exchange loss	$(0.9)	$(0.2)	$(0.8)	$(0.2)
Unrealized gains on company-owned life insurance contracts and investments held in rabbi trusts	0.9	0.3	1.4	0.8
Other	0.2	0.2	0.3	0.4
Total other income, net	$0.2	$0.3	$0.9	$1.0

12. Income Taxes

The effective tax rate used for interim periods is the estimated annual effective consolidated tax rate, based on the current estimate of full year results, except that taxes related to specific events, if any, are recorded in the interim period in which they occur. The annual effective tax rate is based upon a number of significant estimates and judgments, including the estimated annual pre-tax income of the Company in each tax jurisdiction in which it operates, and the development of tax planning strategies during the year. In addition, the Company's tax expense can be impacted by changes in tax rates or laws, the finalization of tax audits, and other factors that cannot be predicted with certainty. As such there can be significant volatility in interim tax provisions.

Income tax expense for the three months ended December 31, 2017 was a benefit of $58.4 million, or negative 173.3 percent of pre-tax income as compared with expense of $1.3 million, or 15.7 percent of pre-tax income for the three months ended December 31, 2016. Income tax expense for the six months ended December 31, 2017 was a benefit of $46.6 million or negative 67.6 percent of pre-tax income as compared with expense of $2.2 million, or 73.3 percent of pre-tax income for the six months ended December 31, 2016.

An Act to Provide for Reconciliation Pursuant to Titles II and V of the Concurrent Resolution on the Budget for Fiscal Year 2018" (the "Act") was enacted on December 22, 2017. The Act includes provisions that reduce the federal corporate income tax rate, create a territorial tax system with a one-time mandatory tax on previously deferred foreign earnings (i.e. transition tax), and change certain business deductions including allowing for immediate expensing of certain qualified capital expenditures. The permanent reduction to the U.S. federal corporate income tax rate from 35% to 21% is effective January 1, 2018. Based on the provisions of the Act, during the quarter ended December 31, 2017, the Company's estimated annual effective tax rate was adjusted to incorporate the lower federal tax rate that will be phased in for fiscal year 2018. The Company also recorded discrete income tax net benefits of $66.0 million during the quarter ended December 31, 2017. Included in this benefit are a $73.3 million tax benefit to reflect the impact of the re-measurement of deferred tax assets and liabilities at the reduced federal tax rate, $5.1 million expense for the transition tax and income tax expense of $2.2 million for increases in certain state valuation allowances for deferred tax assets resulting from the impact of a state law change that will limit the Company's ability to utilize state net operating loss carryforwards.

The Company determined that the amounts recorded for the liability associated transition tax are provisional because various components of the computation are not yet finalized as of December 31, 2017, including the following significant items: the actual aggregate foreign cash position and the earnings and profits of the foreign entities as of June 30, 2018, the interpretation and identification of cash positions as of June 30, 2018, and computations of accumulated earnings and profits balances as of November 2, 2017 and December 31, 2017. Under the Act, the transition tax will be paid over an eight year period beginning in fiscal year 2019.

The Company also determined that the re-measurement of deferred tax assets and liabilities at the lower federal corporate income tax rate is provisional until such time that the underlying temporary differences are known rather than estimated.

Future adjustments to the provisional amounts related to the Act will be recorded as discrete adjustments to income tax expense in the period in which those adjustments are determined.

Income tax expense for the three months ended December 31, 2016 includes tax benefits of $0.9 million associated with the repatriation of earnings from one of our foreign subsidiaries. Income tax expense also includes a $0.3 million benefit primarily due to additional research and development credits claimed in the prior year.

In October 2016, the Company made a voluntary pension contribution of $100.0 million that was announced in connection with the plan freeze. As a result of the pension contribution, income tax expense in the six months ended December 31, 2016 included a discrete tax charge of $2.1 million due to reduced tax benefits for domestic manufacturing claimed in prior periods.

As of June 30, 2017, the Company had $99.1 million of indefinitely reinvested foreign earnings for which deferred income taxes had not been provided. Given the Act's significant changes and potential opportunities to repatriate cash tax free, the Company is in the process of evaluating its assertions for indefinite reinvestment.

13. Business Segments

The Company has two reportable segments, Specialty Alloys Operations ("SAO") and Performance Engineered Products ("PEP").

The SAO segment is comprised of the Company's major premium alloy and stainless steel manufacturing operations. This includes operations performed at mills primarily in Reading and Latrobe, Pennsylvania and surrounding areas as well as South Carolina and Alabama. The combined assets of the SAO operations are being managed in an integrated manner to optimize efficiency and profitability across the total system.

The PEP segment is comprised of the Company's differentiated operations. This segment includes the Dynamet titanium business, the Carpenter Powder Products business, the Amega West business, and the Latrobe and Mexico distribution businesses. The businesses in the PEP segment are managed with an entrepreneurial structure to promote flexibility and agility to quickly respond to market dynamics.

The Company's executive management evaluates the performance of these operating segments based on sales, operating income and cash flow generation. Segment operating profit excludes general corporate costs, which include executive and director compensation, and other corporate facilities and administrative expenses not allocated to the segments.

The service cost component of the Company's net pension expense, which represents the estimated cost of future pension liabilities earned associated with active employees, is included in the operating income of the business segments. The residual net pension expense, which is comprised of the expected return on plan assets, interest costs on the projected benefit obligations of the plans and amortization of actuarial gains and losses and prior service costs, is included under the heading "Pension earnings, interest and deferrals".

On a consolidated basis, one customer, Arconic Inc., accounted for approximately 10 percent of the net sales for both the three and six months ended December 31, 2017. On a consolidated basis, one customer, Arconic Inc., accounted for approximately 17 percent and 15 percent of the net sales for the three and six months ended December 31, 2016,

respectively. Approximately 22 percent of the accounts receivable outstanding at December 31, 2017 is due from two customers, Arconic Inc. and Precision Castparts Corporation. No single customer accounted for 10 percent or more of the accounts receivable outstanding at June 30, 2017.

Table of Contents

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

Segment Data	Three Months Ended December 31,		Six Months Ended December 31,	
($ in millions)	2017	2016	2017	2016
Net Sales:				
Specialty Alloys Operations	$406.3	$348.6	$803.1	$663.7
Performance Engineered Products	104.8	83.2	205.5	161.7
Intersegment	(23.3)	(4.4)	(41.1)	(9.1)
Consolidated net sales	$487.8	$427.4	$967.5	$816.3

Segment Data	Three Months Ended December 31,		Six Months Ended December 31,	
($ in millions)	2017	2016	2017	2016
Operating Income:				
Specialty Alloys Operations	$49.8	$35.6	$100.3	$60.6
Performance Engineered Products	7.5	0.8	12.8	(2.0)
Corporate costs	(13.9)	(16.0)	(26.9)	(29.8)
Pension earnings, interest and deferrals	(0.5)	(5.6)	(1.1)	(12.7)
Intersegment	(2.1)	0.6	(2.6)	0.7
Consolidated operating income	$40.8	$15.4	$82.5	$16.8

Segment Data	Three Months Ended December 31,		Six Months Ended December 31,	
($ in millions)	2017	2016	2017	2016
Depreciation and Amortization:				
Specialty Alloys Operations	$23.4	$23.7	$46.5	$47.2
Performance Engineered Products	5.1	5.2	10.1	10.3
Corporate	0.9	0.9	1.8	1.7
Intersegment	(0.2)	0.1	(0.4)	(0.5)
Consolidated depreciation and amortization	$29.2	$29.9	$58.0	$58.7

Segment Data	Three Months Ended December 31,		Six Months Ended December 31,	
($ in millions)	2017	2016	2017	2016
Capital Expenditures:				
Specialty Alloys Operations	$11.2	$8.3	$28.4	$23.0
Performance Engineered Products	6.3	2.5	11.1	7.0
Corporate	9.6	7.7	16.7	15.2
Intersegment	(0.3)	—	(0.5)	(0.1)
Consolidated capital expenditures	$26.8	$18.5	$55.7	$45.1

Segment Data	December 31,	June 30,
($ in millions)	2017	2017
Total Assets:		

Specialty Alloys Operations	$ 2,337.9	$2,292.1
Performance Engineered Products	475.7	434.3
Corporate	148.4	167.2
Intersegment	(17.9)	(15.5)
Consolidated total assets	$ 2,944.1	$2,878.1

21

14. Recent Accounting Pronouncements

Recently Issued Accounting Pronouncements - Adopted in current period

In March 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2016-09, Compensation — Stock Compensation (Topic 718) - Improvements to Employee Share-Based Payment Accounting, which outlines new provisions intended to simplify various aspects related to accounting for share-based payments and their presentation in the financial statements. The update revises requirements in the following areas: income tax consequences, forfeitures and classification on the statement of cash flows. The Company adopted this standard in the quarter ended September 30, 2017. The standard did not have a material impact on the consolidated financial statements of the Company. The amendments requiring recognition of excess tax benefits and tax deficiencies in the income statement will be applied prospectively. The inclusion of excess tax benefits and deficiencies as a component of income tax expense will increase volatility of the provision for income taxes as the amount of excess tax benefits or deficiencies from share-based compensation awards are dependent on the stock price at the date the awards are exercised or vested. The Company does not expect the impact to be material to the Company’s consolidated results of operations; however, such determination is subject to change based on facts and circumstances at the time when awards vest or settle. The Company accounts for forfeitures of share-based awards when they occur. The Company applied the amendments related to the presentation of excess tax benefits on the consolidated statement of cash flows using a prospective transition method, and as a result, excess tax benefits related to share-based awards will be reported as cash flows from operating activities. The Company applied the amendments related to the presentation of statutory tax withholding on the consolidated statement of cash flows using a retrospective transition method as required, and as a result, statutory tax withholding related to share-based awards which had been previously classified as cash flows used for operating activities has been be reclassified as cash flows used for financing activities.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230) - Classification of Certain Cash Receipts and Cash Payments, which outlines new provisions intended to reduce the existing diversity in practice related to accounting for the cash flow and its presentation in the financial statements. ASU 2016-15 is effective for public business entities for annual periods, including interim periods within those annual periods, beginning after December 15, 2017, with early adoption permitted. The Company adopted the provisions of ASU 2016-15 in the quarter ended September 30, 2017. The adoption of ASU 2016-15 did not materially impact the Company’s consolidated statement of cash flows.

In November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230) - Restricted Cash, which outlines that a statement of cash flows explains the change during the period in total cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. ASU 2016-18 is effective for public business entities for annual periods, including interim periods within those annual periods, beginning after December 15, 2017, with early adoption permitted. The Company adopted the provisions of ASU 2016-18 in the quarter ended September 30, 2017. The adoption of ASU 2016-18 did not materially impact the Company’s consolidated statement of cash flows.

In January 2017, the FASB issued ASU 2017-04, Intangibles - Goodwill and Other (Topic 350) - Simplifying the Test for Goodwill Impairment, which outlines updates to simplify the subsequent measurement of goodwill by eliminating Step 2 from the goodwill impairment test. ASU 2017-04 is effective for public business entities for annual periods,

including interim periods within those annual periods, beginning after December 15, 2019, with early adoption permitted. The Company adopted ASU 2017-04 in the quarter ended September 30, 2017. The adoption of ASU 2017-04 did not have an impact on the Company’s financial statements.

Recently Issued Accounting Pronouncements - Pending Adoption

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606). The guidance in ASU 2014-09 requires that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance in ASU 2014-09 permits two methods of adoption: full retrospective in which the standard is applied to all of the periods presented or modified retrospective where an entity would recognize the cumulative effect of initially applying the standard as an adjustment to the opening balance of retained earnings. The adoption will include updates as provided under ASU 2016-08, Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net); ASU 2016-10, Revenue from Contracts with Customers: Identifying Performance Obligations and Licensing; ASU 2016-12, Revenue from Contracts with Customers: Narrow-Scope Improvements and Practical Expedients; ASU 2016-20, Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers; ASU 2017-13, Revenue Recognition (Topic 605), Revenue from Contracts with Customers (Topic 606), Leases (Topic 840), and Leases (Topic 842): Amendments to SEC Paragraphs Pursuant to the Staff Announcement at the July 20, 2017 EITF Meeting and Rescission of Prior SEC Staff Announcements and Observer Comments and ASU 2017-14, Income Statement-Reporting Comprehensive Income (Topic 220), Revenue Recognition (Topic 605), and Revenue from Contracts with Customers (Topic 606).

The Company is in the process of evaluating the effect that Topic 606 will have on its Consolidated Financial Statements and related disclosures, as well as the expected method of adoption. Currently, the Company is in the process of completing the assessment phase of its evaluation. The assessment phase includes conducting and evaluating the results of internal surveys of its businesses, holding revenue recognition workshops with commercial and business unit finance leadership, and reviewing revenue arrangements across all businesses to initially identify a set of applicable qualitative revenue recognition changes related to the standards update. The Company's method of adoption for Topic 606 has not yet been determined and is not expected to be finalized until the assessment phase of the evaluation has been completed. The Company's effective date for the adoption of Topic 606 is July 1, 2018.

In February 2016, the FASB issued ASU 2016-02 Leases (Topic 842). ASU 2016-02 improves transparency and comparability among companies by recognizing lease assets and lease liabilities on the balance sheet and by disclosing key information about leasing arrangements. ASU 2016-02 is effective for public business entities for annual periods, including interim periods within those annual periods, beginning after December 15, 2018, with early adoption permitted. The Company is evaluating the impact of the adoption of ASU 2016-02 on the consolidated financial statements.

In October 2016, the FASB issued ASU 2016-16, Income Taxes (Topic 740) - Intra-Entity Transfers of Assets Other Than Inventory, which outlines updates to improve the accounting for the income tax consequences of intra-entity transfers of assets other than inventory. ASU 2016-16 is effective for public business entities for annual periods, including interim periods within those annual periods, beginning after December 15, 2017, with early adoption permitted. The Company is evaluating the impact of the adoption of ASU 2016-16 on the consolidated financial statements.

In March 2017, the FASB issued ASU 2017-07, Compensation - Retirement Benefits (Topic 715) - Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost, which outlines updates to improve the presentation of net periodic pension cost and net periodic postretirement benefit cost. ASU 2017-07 is

effective for public business entities for annual periods, including interim periods within those annual periods, beginning after December 15, 2017, with early adoption permitted. The Company is evaluating the impact of the adoption of ASU 2017-07 on the consolidated financial statements.

In August 2017, the FASB issued ASU 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities, which expands and refines hedge accounting for both financial and non-financial risk components, aligns the recognition and presentation of the effects of hedging instruments and hedge items in the financial statements, and includes certain targeted improvements to ease the application of current guidance related to the assessment of hedge effectiveness. ASU 2017-12 is effective for public business entities for annual periods, including interim periods within those annual periods, beginning after December 15, 2018, with early adoption permitted. The Company is evaluating the impact of the adoption of ASU 2017-12 on the consolidated financial statements.

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

15. Reclassifications from Accumulated Other Comprehensive Income (Loss) (AOCI)

The changes in AOCI by component, net of tax, for the three months ended December 31, 2017 and 2016 were as follows:

Three Months Ended December 31, 2017 ($ in millions) (a)	Cash flow hedging items	Pension and other postretirement benefit plan items	Unrealized losses on available-for-sale securities	Foreign currency items	Total
Balance at September 30, 2017	$ 5.8	$ (296.9)	$ (0.3)	$ (39.7)	$ (331.1)
Other comprehensive income (loss) before reclassifications	14.9	—	—	(1.5)	13.4
Amounts reclassified from AOCI (b)	0.1	2.5	—	—	2.6
Net other comprehensive income (loss)	15.0	2.5	—	(1.5)	16.0
Balance at December 31, 2017	$ 20.8	$ (294.4)	$ (0.3)	$ (41.2)	$ (315.1)

Three Months Ended December 31, 2016 ($ in millions) (a)	Cash flow hedging items	Pension and other postretirement benefit plan items	Unrealized losses on available-for-sale securities	Foreign currency items	Total
Balance at September 30, 2016	$ (11.0)	$ (326.9)	$ (0.3)	$ (44.2)	$ (382.4)
Other comprehensive loss before reclassifications	(0.6)	—	—	(4.0)	(4.6)
Amounts reclassified from AOCI (b)	4.4	5.7	—	—	10.1
Net other comprehensive income (loss)	3.8	5.7	—	(4.0)	5.5
Balance at December 31, 2016	$ (7.2)	$ (321.2)	$ (0.3)	$ (48.2)	$ (376.9)

(a) All amounts are net of tax. Amounts in parentheses indicate debits.
(b) See separate table below for further details.

The changes in AOCI by component, net of tax, for the six months ended December 31, 2017 and 2016 were as follows:

Six Months Ended December 31, 2017 ($ in millions) (a)	Cash flow hedging items	Pension and other postretirement benefit plan items	Unrealized losses on available-for-sale securities	Foreign currency items	Total
Balance at June 30, 2017	$ (2.3)	$ (299.0)	$ (0.3)	$ (41.5)	$ (343.1)
Other comprehensive income before reclassifications	21.0	—	—	0.3	21.3
Amounts reclassified from AOCI (b)	2.1	4.6	—	—	6.7
Net other comprehensive income	23.1	4.6	—	0.3	28.0
Balance at December 31, 2017	$ 20.8	$ (294.4)	$ (0.3)	$ (41.2)	$ (315.1)

24

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

Six Months Ended December 31, 2016 ($ in millions) (a)	Cash flow hedging items	Pension and other postretirement benefit plan items	Unrealized losses on available-for-sale securities	Foreign currency items	Total
Balance at June 30, 2016	$ (21.8)	$ (344.3)	$ (0.3)	$ (43.5)	$ (409.9)
Other comprehensive income (loss) before reclassifications	3.9	11.4	—	(4.7)	10.6
Amounts reclassified from AOCI (b)	10.7	11.7	—	—	22.4
Net current-period other comprehensive income (loss)	14.6	23.1	—	(4.7)	33.0
Balance at December 31, 2016	$ (7.2)	$ (321.2)	$ (0.3)	$ (48.2)	$ (376.9)

(a) All amounts are net of tax. Amounts in parentheses indicate debits.
(b) See separate table below for further details.

Table of Contents

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

The following is a summary of amounts reclassified from AOCI for the three and six months ended December 31, 2017 and 2016:

($ in millions) (a)	Location of (loss) gain	Amount Reclassified from AOCI Three Months Ended December 31,		Amount Reclassified from AOCI Six Months Ended December 31,	
Details about AOCI Components		2017	2016	2017	2016