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VALHI INC /DE/
Form 10-Q
August 07, 2006

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarter ended June 30, 2006 Commission file number 1-5467

VALHI, INC.
(Exact name of Registrant as specified in its charter)

Delaware 87-0110150

(State or other jurisdiction of (IRS Employer
incorporation or organization) Identification No.)

5430 LBJ Freeway, Suite 1700, Dallas, Texas 75240-2697
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (972) 233-1700

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

Whether the Registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer (as defined in Rule 12b-2 of the Act). Large accelerated filer Accelerated filer X non-accelerated filer .

Whether the Registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No X .
--- ---

Number of shares of the Registrant's common stock outstanding on July 31, 2006: 115,477,878.

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VALHI, INC. AND SUBSIDIARIES

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Items 3 and 5 of Part II are omitted because there is no information to report.

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VALHI, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED BALANCE SHEETS
 (In thousands)

ASSETS	December 31, 2005

Current assets:	
Cash and cash equivalents	\$ 274,963
Restricted cash equivalents	6,007
Marketable securities	11,755
Accounts and other receivables, net	218,766
Refundable income taxes	1,489
Receivable from affiliates	34
Inventories, net	283,157
Prepaid expenses	9,981
Deferred income taxes	10,502

Total current assets	816,654

Other assets:	
Marketable securities:	
The Amalgamated Sugar Company LLC	250,000
Other	8,705
Investment in affiliates	270,632
Unrecognized net pension obligations	11,916
Prepaid pension costs	3,529
Goodwill	361,783
Other intangible assets	3,432
Deferred income taxes	213,726
Other	61,639

Total other assets	1,185,362

Property and equipment:	
Land	37,876
Buildings	220,110
Equipment	827,690
Mining properties	19,969
Construction in progress	15,771

Less accumulated depreciation	1,121,416
	545,055

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Net property and equipment	576,361 -----
Total assets	\$2,578,377 =====

VALHI, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS (CONTINUED)

(In thousands)

LIABILITIES AND STOCKHOLDERS' EQUITY	December 31, 2005 -----
Current liabilities:	
Current maturities of long-term debt	\$ 1,615
Accounts payable	105,650
Accrued liabilities	129,429
Payable to affiliates	13,754
Income taxes	24,680
Deferred income taxes	4,313 -----
Total current liabilities	279,441 -----
Noncurrent liabilities:	
Long-term debt	715,820
Accrued pension costs	140,742
Accrued OPEB costs	32,279
Accrued environmental costs	49,161
Deferred income taxes	400,964
Other	39,328 -----
Total noncurrent liabilities	1,378,294 -----
Minority interest	125,049 -----
Stockholders' equity:	
Common stock	1,207
Additional paid-in capital	108,810
Retained earnings	786,268
Accumulated other comprehensive income:	
Marketable securities	4,194
Currency translation	11,157
Pension liabilities	(78,101)
Treasury stock	(37,942)

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Total stockholders' equity	795,593
Total liabilities, minority interest and stockholders' equity	\$2,578,377

Commitments and contingencies (Notes 12 and 15)

See accompanying Notes to Condensed Consolidated Financial Statements.

VALHI, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(In thousands, except per share data)

	Three months ended June 30,		Si
	2005	2006	
			(unaudited)
Revenues and other income:			
Net sales	\$359,444	\$399,552	\$700,691
Other income, net	19,408	10,303	46,045
Equity in earnings of:			
Titanium Metals Corporation ("TIMET")	15,790	20,339	32,591
Other	(291)	(238)	(179)
	-----	-----	-----
Total revenue and other income	394,351	429,956	779,148
	-----	-----	-----
Costs and expenses:			
Cost of sales	259,903	308,486	511,885
Selling, general and administrative	54,192	59,837	108,623
Loss on prepayment of debt	-	22,311	-
Interest	17,777	19,176	35,656
	-----	-----	-----
Total costs and expenses	331,872	409,810	656,164
	-----	-----	-----
Income before income taxes	62,479	20,146	122,984
Provision for income taxes (benefit)	29,376	(561)	59,322
Minority interest in after-tax earnings	4,800	2,315	10,297

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	-----	-----	-----
Income from continuing operations	28,303	18,392	53,365
Discontinued operations, net of tax	-	(147)	(272)
	-----	-----	-----
Net income	\$ 28,303	\$ 18,245	\$ 53,093
	=====	=====	=====
Basic earnings per share:			
Income from continuing operations	\$.24	\$.16	\$.45
Discontinued operations	-	-	-
	-----	-----	-----
Net income	\$.24	\$.16	\$.45
	=====	=====	=====
Diluted earnings per share:			
Income from continuing operations	\$.24	\$.16	\$.44
Discontinued operations	-	-	-
	-----	-----	-----
Net income	\$.24	\$.16	\$.44
	=====	=====	=====
Cash dividends per share	\$.10	\$.10	\$.20
	=====	=====	=====
Shares used in the calculation of per share amounts:			
Basic earnings per common share	118,027	116,395	119,125
Dilutive impact of outstanding stock options	382	396	366
	-----	-----	-----
Diluted earnings per share	118,409	116,791	119,491
	=====	=====	=====

See accompanying Notes to Condensed Consolidated Financial Statements.

VALHI, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Six months ended June 30, 2005 and 2006

(In thousands)

	2005

	(unaud)
Net income	\$53,093

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Other comprehensive income (loss), net of tax:	
Marketable securities adjustment	(166)
Currency translation adjustment	(2,794)

Total other comprehensive income (loss), net	(2,960)

Comprehensive income	\$50,133
	=====

See accompanying Notes to Condensed Consolidated Financial Statements.

VALHI, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

Six months ended June 30, 2005 and 2006

(In thousands)

Cash flows from operating activities:	
Net income	\$ 53
Depreciation and amortization	37
Goodwill impairment	
Securities transactions, net	(20)
Loss on prepayment of debt	
Call premium paid on Senior Secured Notes	
Benefit plan expense less then cash funding:	
Defined benefit pension expense	(3)
Other postretirement benefit expense	(1)
Deferred income taxes:	
Continuing operations	19
Discontinued operations	
Minority interest:	
Continuing operations	10
Discontinued operations	
Other, net	
Equity in:	
TIMET	(32)
Other	
Net distributions from (contributions to):	
Manufacturing joint venture	
Other	

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Change in assets and liabilities:	
Accounts and other receivables, net	(54)
Inventories, net	(19)
Accounts payable and accrued liabilities	(15)
Accounts with affiliates	5
Income taxes	(1)
Other, net	(5)

Net cash used in operating activities	(26)

Cash flows from investing activities:	
Capital expenditures	(25)
Purchases of:	
Kronos common stock	(3)
TIMET common stock	(17)
CompX common stock	
Business unit, net of cash acquired	
Marketable securities	(16)
Capitalized permit costs	(1)
Proceeds from disposal of:	
Business unit	18
Kronos common stock	19
Marketable securities	6
Interest in Norwegian smelting operation	3
Cash of disposed business unit	(4)
Loans to affiliate, net	6
Change in restricted cash equivalents, net	3
Other, net	

Net cash used in investing activities	(11)

VALHI, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)

Six months ended June 30, 2005 and 2006

(In thousands)

	2005

	(unaud)
Cash flows from financing activities:	
Indebtedness:	
Borrowings	\$ 78
Principal payments	(13,134)
Deferred financing costs paid	(28)
Valhi dividends paid	(24,621)
Distributions to minority interest	(5,007)
Treasury stock acquired	(41,822)

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NL common stock issued	2,693
Issuance of Valhi common stock and other, net	1,435

Net cash provided by (used in) financing Activities	(80,406)

Cash and cash equivalents - net change from:	
Operating, investing and financing activities	(118,620)
Currency translation	(1,020)
Cash and equivalents at beginning of period	267,829

Cash and equivalents at end of period	\$ 148,189
	=====
Supplemental disclosures:	
Cash paid for:	
Interest, net of amounts capitalized	\$ 35,559
Income taxes, net	36,885
Noncash investing activities:	
Note receivable received upon disposal of business unit	\$ 4,179
Inventories received as partial consideration for disposal of interest in Norwegian smelting operation	\$ 1,897

See accompanying Notes to Condensed Consolidated Financial Statements.

VALHI, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

Six months ended June 30, 2006

(In thousands)

Common stock	Additional paid-in capital	Retained earnings	Accumulated other comprehensive Marketable securities	Currency translation	Pen liabi
-----	-----	-----	-----	-----	-----
				(unaudited)	

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Balance at December 31, 2005	\$1,207	\$108,810	\$786,268	\$4,194	\$11,157	\$ (78
Net income	-	-	41,109	-	-	-
Dividends	-	-	(24,110)	-	-	-
Other comprehensive income, net	-	-	-	481	18,373	-
Treasury stock:						
Acquired	-	-	-	-	-	-
Retired	(5)	(457)	(9,711)	-	-	-
Other, net	1	237	-	-	-	-
	-----	-----	-----	-----	-----	-----
Balance at June 30, 2006	\$1,203	\$108,590	\$793,556	\$ 4,675	\$29,530	\$ (78
	=====	=====	=====	=====	=====	=====

See accompanying Notes to Condensed Consolidated Financial Statements.

VALHI, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2006

(unaudited)

Note 1 - Organization and basis of presentation:

Organization - We are majority owned by Contran Corporation, which directly or through its subsidiaries owns approximately 92% of our outstanding common stock at June 30, 2006. Substantially all of Contran's outstanding voting stock is held by trusts established for the benefit of certain children and grandchildren of Harold C. Simmons (for which Mr. Simmons is the sole trustee) or is held directly by Mr. Simmons or other persons or related companies to Mr. Simmons. Consequently, Mr. Simmons may be deemed to control Contran and us.

Basis of Presentation - Consolidated in this Quarterly Report are the results of our majority-owned and wholly-owned subsidiaries, including NL Industries, Inc., Kronos Worldwide, Inc., CompX International, Inc., Tremont LLC and Waste Control Specialists LLC ("WCS"). We also own a non-controlling interest in Titanium Metals Corporation ("TIMET") that we account for by the equity method. Kronos (NYSE: KRO), NL (NYSE: NL), CompX (NYSE: CIX) and TIMET (NYSE: TIE) each file periodic reports with the Securities and Exchange Commission ("SEC").

The unaudited Condensed Consolidated Financial Statements contained in this Quarterly Report have been prepared on the same basis as the audited Consolidated Financial Statements included in our Annual Report on Form 10-K for the year ended December 31, 2005 that we filed with the SEC on March 24, 2006 (the "2005 Annual Report"). In our opinion, we have made all necessary adjustments (which include only normal recurring adjustments) in order to state fairly, in all material respects, our consolidated financial position, results

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of operations and cash flows as of the dates and for the periods presented. We have condensed the Consolidated Balance Sheet at December 31, 2005 contained in this Quarterly Report as compared to our audited Consolidated Financial Statements at that date, and we have omitted certain information and footnote disclosures (including those related to the Consolidated Balance Sheet at December 31, 2005) normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"). Our results of operations for the interim periods ended June 30, 2006 may not be indicative of our operating results for the full year. The Condensed Consolidated Financial Statements contained in this Quarterly Report should be read in conjunction with our 2005 Consolidated Financial Statements contained in our 2005 Annual Report.

Unless otherwise indicated, references in this report to "we", "us" or "our" refer to Valhi, Inc and its subsidiaries, taken as a whole.

Note 2 - Business segment information:

Business segment	Entity	Our % ownership at June 30, 2006
Chemicals	Kronos	95%
Component products	CompX	70%
Waste management	WCS	100%
Titanium metals	TIMET	35%

Our ownership of Kronos includes 59% we hold directly and 36% held directly by NL. We own 83% of NL. During the first six months of 2006, we purchased approximately 926,000 shares of Kronos common stock in market transactions for an aggregate purchase price of \$25.2 million. We accounted for this purchase as a step acquisition under the purchase method of accounting.

Our ownership of CompX is primarily through CompX Group, Inc, a majority-owned subsidiary of NL. NL owns 82.4% of CompX Group, and TIMET owns the remaining 17.6% of CompX Group. CompX Group's sole asset is 83% of the outstanding common stock of CompX. NL also owns an additional 2% of CompX directly. During the first six months of 2006, NL purchased approximately 117,000 shares of CompX common stock in market transactions for an aggregate purchase price of \$1.8 million. NL accounted for this purchase as a step acquisition under the purchase method of accounting.

We own 31% of TIMET through a wholly-owned subsidiary, and we directly own an additional 4% of TIMET. During the first six months of 2006, we purchased approximately 543,000 shares of TIMET common stock for an aggregate purchase price of \$17.0 million. TIMET owns an additional 3% of CompX, .5% of NL and less than .1% of Kronos. Because we do not consolidate TIMET, the shares of CompX Group, CompX, NL and Kronos held by TIMET are not considered as being owned by us for financial reporting purposes.

	Three months ended June 30,		Six months ended
	2005	2006	2005
	----	----	----
Net sales:			
Chemicals	\$311.7	\$345.1	\$603.6
Component products	45.8	50.2	92.6

(In millions)

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Waste management	2.0	4.3	4.5
	-----	-----	-----
Total net sales	\$359.5	\$399.6	\$700.7
	=====	=====	=====
Cost of goods sold:			
Chemicals	\$220.8	\$266.8	\$432.4
Component products	35.2	37.8	71.8
Waste management	3.9	3.8	7.7
	-----	-----	-----
	\$259.9	\$308.4	\$511.9
	=====	=====	=====
Gross margin*:			
Chemicals	\$ 90.9	\$ 78.3	\$171.2
Component products	10.6	12.4	20.8
Waste management	(1.9)	.5	(3.2)
	-----	-----	-----
	\$ 99.6	\$ 91.2	\$188.8
	=====	=====	=====
Operating income:			
Chemicals	\$ 55.1	\$ 34.3	\$ 98.7
Component products	4.8	5.7	8.9
Waste management	(3.5)	(1.1)	(6.3)
	-----	-----	-----
Total operating income	56.4	38.9	101.3
Equity in:			
TIMET	15.8	20.4	32.6
Other	(.3)	(.3)	(.2)
General corporate items:			
Interest and dividend income	9.3	10.6	19.5
Securities transaction gains, net	5.6	-	20.2
Insurance recoveries	1.2	.6	1.2
General expenses, net	(7.7)	(8.6)	(15.9)
Loss on prepayment of debt	-	(22.3)	-
Interest expense	(17.8)	(19.2)	(35.7)
	-----	-----	-----
Income before income taxes	\$ 62.5	\$ 20.1	\$123.0
	=====	=====	=====

*Sales less cost of goods sold.

In April 2006, CompX completed an acquisition of a Marine component products business for aggregate cash consideration of \$9.8 million, net of cash acquired. We completed this acquisition to expand the Marine component products business unit of CompX. We have included the results of operations and cash flows of the acquired business in our Condensed Consolidated Financial Statements starting in April 2006. The purchase price has been allocated among the tangible and intangible net assets acquired based upon an estimate of the fair value of such net assets. The pro forma effect to us, assuming this immaterial acquisition had been completed as of January 1, 2005, is not material.

Segment results we report may differ from amounts separately reported by

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our various subsidiaries and affiliates due to purchase accounting adjustments and related amortization or differences in the way we define operating income. Intersegment sales are not material.

Note 3 - Accounts and other receivables, net:

	December 31, 2005 ----- (In thousand)
Accounts receivable	\$211,156
Notes receivable	4,267
Accrued interest and dividends receivable	6,158
Allowance for doubtful accounts	(2,815) -----
Total	\$218,766 =====

Note 4 - Inventories, net:

	December 31, 2005 ----- (In thousand)
Raw materials:	
Chemicals	\$ 52,343
Component products	7,022 -----
Total raw materials	59,365 -----
In-process products:	
Chemicals	17,959
Component products	9,898 -----
Total in-process products	27,857 -----
Finished products:	
Chemicals	150,675
Component products	5,542 -----
Total finished products	156,217 -----
Supplies (primarily chemicals)	39,718 -----

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Total	\$283,157
	=====

Note 5 - Other assets:

	December 31, 2005

	(In thousand)
Investment in affiliates:	
TIMET:	
Common stock	\$138,677
Preferred stock	183

	138,860
TiO2 manufacturing joint venture	115,308
Other	16,464

Total	\$270,632
	=====
Other noncurrent assets:	
IBNR receivables	\$ 16,735
Waste disposal site operating permits, net	14,133
Deferred financing costs	8,278
Loans and other receivables	2,502
Restricted cash equivalents	382
Other	19,609

Total	\$ 61,639
	=====

At June 30, 2006, we held 56.5 million shares of TIMET with a quoted market price of \$34.38 per share, or an aggregate market value of \$1.9 billion. The 56.5 million shares of TIMET we held reflect the effects of 2:1 stock splits TIMET implemented in each of February and May 2006.

Certain selected financial information of TIMET is summarized below:

December 31, 2005

(In millions)

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Current assets	\$550.3
Property and equipment	253.0
Marketable securities	46.5
Investment in joint ventures	26.0
Other noncurrent assets	31.5

Total assets	\$907.3
	=====
Current liabilities	\$166.9
Accrued pension and post retirement benefits	74.0
Long-term debt	51.4
Other non current liabilities	39.3
Minority interest	13.5
Stockholders' equity	562.2

Total liabilities and stockholders' equity	\$907.3
	=====

	Three months ended June 30,	
	2005	2006
	-----	-----
Net sales	\$183.7	\$300.9
Cost of sales	135.8	194.6
Operating income	36.9	93.5
Net income attributable to common stockholders	33.6	54.3

(In m

Note 6 - Accrued liabilities:

	December 31, 2005

Current:	
Employee benefits	\$ 48,341
Environmental costs	16,565
Deferred income	5,101
Interest	1,067
Other	58,355

(In thousa

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Total	\$129,429
	=====
Noncurrent:	
Insurance claims and expenses	\$ 24,257
Employee benefits	4,998
Asset retirement obligations	1,381
Deferred income	573
Other	8,119

Total	\$ 39,328
	=====

Note 7 - Long-term debt:

	December 31, 2005

	(In thousands)
Valhi - Snake River Sugar Company	\$250,000

Subsidiary debt:	
Kronos International:	
6.5% Senior Secured Notes	-
8.875% Senior Secured Notes	449,298
Kronos U.S. bank credit facility	11,500
Kronos Canadian bank credit facility	-
Other	6,637

Total subsidiary debt	467,435

Total debt	717,435
Less current maturities	1,615

Total long-term debt	\$715,820
	=====

Senior Secured Notes - In May 2006, we redeemed our 8.875% Senior Secured Notes at 104.437% of their aggregate principal amount of euro 375 million for an aggregate of \$491.4 million, including the \$20.9 million call premium. We funded the redemption of our 8.875% Notes through our April 2006 issuance of euro 400 million principal amount of 6.5% Senior Secured Notes due in 2013. Our 6.5% Notes were issued at 99.306% of the principal amount (\$498.5 when issued). The covenants, restrictions and collateral requirements of the new 6.5% Notes are substantially identical to those of the 8.875% Notes. We recognized a \$22.3 million pre-tax interest expense charge in the second quarter of 2006 for the early extinguishment of the 8.875% Senior Secured Notes. The charge includes the

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call premium and the write-off of deferred financing costs and unamortized premium on the 8.875% Notes.

Revolving Credit Facilities - During the first six months of 2006, we borrowed a net Cdn. \$5.0 million (\$4.5 million) under Kronos' Canadian revolving credit facility and a net \$20.8 million under Kronos' U.S. bank credit facility. The average interest rates on the outstanding balance under these facilities at June 30, 2006 were 6.75% and 8.25%, respectively.

Note 8 - Employee benefit plans:

Defined Benefit Plans - The components of net periodic defined benefit pension cost are presented in the table below.

	Three months ended June 30,		Six
	2005	2006	2005

(In thousands)			
Service cost	\$ 1,914	\$ 1,991	\$ 3,9
Interest cost	5,675	5,941	11,4
Expected return on plan assets	(5,632)	(6,405)	(11,3
Amortization of prior service cost	150	114	3
Amortization of net transition obligations	135	127	2
Recognized actuarial losses	1,126	2,259	2,2
	-----	-----	-----
Total	\$ 3,368	\$ 4,027	\$ 6,8
	=====	=====	=====

Postretirement Benefits - The components of net periodic postretirement benefit cost are presented in the table below.

	Three months ended June 30,		Six
	2005	2006	2005

(In thousands)			
Service cost	\$ 54	\$ 71	\$ 10
Interest cost	483	473	96
Amortization of prior service credit	(231)	(90)	(46
Recognized actuarial losses (gains)	(34)	29	(17
	-----	-----	-----
Total	\$ 272	\$ 483	\$ 43
	=====	=====	=====

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Plan Assets Invested in Related Parties - The Combined Master Retirement Trust ("CMRT") is a collective investment trust sponsored by Contran to permit the collective investment by certain master trusts which fund certain employee benefits plans sponsored by Contran and certain of its affiliates, including certain plans we maintain. The CMRT owned 10% of TIMET's outstanding common stock and .1% of our outstanding common stock at June 30, 2006. Because we do not consolidate the CMRT, the shares of TIMET and Valhi owned by the CMRT are not considered as being owned by us for financial reporting purposes.

I Contributions - We expect our 2006 contributions for our pension and post retirement benefit plans to be consistent with the amount we disclosed in our 2005 Annual Report.

Note 9 - Accounts with affiliates:

	December 31, 2005 ----- (In thousand)
Current receivables from affiliates:	
Contran - income taxes, net	\$ 33
Other	1 -----
Total	\$ 34 =====
Payables to affiliates:	
Louisiana Pigment Company	\$ 9,803
Contran - trade items	3,940
Contran - income taxes, net	-
Other, net	11 -----
Total	\$13,754 =====

Note 10 - Stockholders' equity:

In March 2005, our board of directors authorized the repurchase of up to 5.0 million shares of our common stock in open market transactions, including block purchases, or in privately negotiated transactions, which may include transactions with our affiliates or subsidiaries. The stock may be purchased from time to time as market conditions permit. The stock repurchase program does not include specific price targets or timetables and may be suspended at any time. Depending on market conditions, we may terminate the program prior to completion. We will use cash on hand to acquire the shares. Repurchased shares could be retired and cancelled or may be added to our treasury stock and used for employee benefit plans, future acquisitions or other corporate purposes.

During the first six months of 2006, we purchased an aggregate of 506,000 shares of our common stock in market transactions for an aggregate of \$10.2 million. At June 30, 2006, these 506,000 treasury shares had been cancelled, and the aggregate \$10.2 million cost was allocated to common stock at par value, additional paid-in capital and retained earnings in accordance with GAAP. At June 30, 2006, approximately 982,000 shares were available for purchase under the repurchase authorization.

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Note 11 - Other income, net:

	Six months June
	----- 2005 -----
	(In thousands)
Securities earnings:	
Dividends and interest	\$19,503
Securities transactions, net	20,205

Total securities earnings	39,708
Currency transactions, net	3,307
Insurance recoveries	1,200
Other, net	1,830

Total other income, net	\$46,045 =====

Note 12 - Provision for income taxes:

	Six months June
	----- 2005 -----
	(In millions)
Expected tax expense	\$43.0
Incremental U.S. tax and rate differences on equity in earnings	11.3
Non-U.S. tax rates	(.3)
Nondeductible expenses	2.1
Resolution of prior year income tax issues, net	-
Income tax on distribution of shares of Kronos common stock	.7
Excess of book basis over tax basis of shares of Kronos common stock sold	1.5
Contingency reserve adjustment, net	.4
Canadian tax rate change	-
U.S. state income taxes, net	.9
Other, net	(.3)

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	\$59.3
	=====
Comprehensive provision for income taxes (benefit) allocated to:	
Income from continuing operations	\$59.3
Discontinued operations	(.4)
Other comprehensive income:	
Marketable securities	.3
Currency translation	(1.5)

	\$57.7
	=====

In June 2006, Canada enacted a 2% reduction in the Canadian federal income tax rate and the elimination of the federal surtax. The 2% reduction will be phased in from 2008 to 2010, and the federal surtax will be eliminated in 2008. As a result, during the second quarter of 2006 we recognized a \$1.3 million income tax benefit related to the effect of such reduction on our previously-recorded net deferred income tax liability with respect to Kronos' and CompX's operations in Canada.

Due to the favorable resolution of certain income tax issues related to Kronos' German and Belgian operations during the first six months of 2006, we recognized a \$2.0 million income tax benefit (\$1 million in the second quarter of 2006) related to adjustments of prior year income taxes.

Tax authorities are examining certain of our non-U.S. tax returns and have or may propose tax deficiencies, including penalties and interest. For example:

- o We previously received a preliminary tax assessment related to 1993 from the Belgian tax authorities proposing tax deficiencies for Kronos, including related interest, of approximately euro 6 million (\$7.2 million at June 30, 2006). The Belgian tax authorities filed a lien on the fixed assets of our Belgian TiO2 operations in connection with their assessment. This lien does not interfere with on-going operations at the facility. We filed a protest to this assessment, and in July 2006 the Belgian tax authorities withdrew the assessment. We expect the lien will be released by the end of 2006.
- o The Norwegian tax authorities previously notified us of their intent to assess tax deficiencies of approximately kroner 12 million (\$2.4 million at June 30, 2006) relating to the years 1998 through 2000 for Kronos. We objected to this proposed assessment, and in May 2006 the Norwegian tax authorities withdrew the assessment.

Principally as a result of the withdrawal of the Belgian and Norwegian assessments discussed above, we have recognized a \$9.2 million income tax benefit in the first six months of 2006 (mostly in the second quarter) related to the total reduction in our income tax contingency reserve. Other income tax examinations related to our operations continue, and we cannot guarantee that these tax matters will be resolved in our favor due to the inherent uncertainties involved in settlement initiatives and court and tax proceedings. We believe we have adequate accruals for additional taxes and related interest expense which could ultimately result from tax examinations. We believe the ultimate disposition of tax examinations should not have a material adverse effect on our consolidated financial position, results of operations or liquidity.

Note 13 - Minority interest:

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	December 31, 2005 -----	(In thousa
Minority interest in net assets:		
NL Industries	\$ 51,177	
Kronos Worldwide	28,167	
CompX International	45,630	
Subsidiary of Kronos	75	

Total	\$125,049 =====	

	Six mont Jun -----	2005 -----	(In tho
Minority interest in net earnings - continuing operations:			
NL Industries		\$ 4,898	
Kronos Worldwide		3,877	
CompX International		1,454	
Subsidiary of Kronos		7	
Subsidiary of NL		61	

Total		\$10,297 =====	

Note 14 - Discontinued operations, net of tax:

Discontinued operations relates to CompX's former Thomas Regout operations in the Netherlands. Prior to December 2004, the Thomas Regout European operations were classified as held for use. A formal plan of disposal adopted by CompX's board of directors in December 2004 resulted in the reclassification of the operations to held for sale. Based upon the estimated realizable value (or fair value less costs to sell) of the net assets disposed, we determined that the goodwill associated with the assets held for sale was partially impaired. In determining the estimated realizable value of the Thomas Regout operations as of December 31, 2004, when we classified it as held for sale, we used the sales price inherent in the definitive agreement reached with the purchaser in January 2005 and our estimate of the related transaction costs (or costs to sell). In January 2005, we completed the sale of Thomas Regout for net proceeds that were approximately \$864,000 less than previously estimated (primarily due to higher expenses associated with the sale). These additional expenses reflect a refinement of our previous estimate of the realizable value of the Thomas Regout operations and accordingly we recognized a further impairment of goodwill. As a result, discontinued operations for the first six months of 2005 includes a charge for the additional expenses (\$272,000, net of income tax benefit and minority interest). Discontinued operations in 2006 represents an expense of

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\$500,000 (\$147,000, net of income tax benefit and minority interest) for our change in estimate of certain indemnification obligations we had to the purchaser of the Thomas Regout operations.

Note 15 - Commitments and contingencies:

Lead pigment litigation - NL

NL's former operations included the manufacture of lead pigments for use in paint and lead-based paint. We, other former manufacturers of lead pigments for use in paint and lead-based paint, and the Lead Industries Association (which discontinued business operations prior to 2005) have been named as defendants in various legal proceedings seeking damages for personal injury, property damage and governmental expenditures allegedly caused by the use of lead-based paints. Certain of these actions have been filed by or on behalf of states, large U.S. cities or their public housing authorities and school districts, and certain others have been asserted as class actions. These lawsuits seek recovery under a variety of theories, including public and private nuisance, negligent product design, negligent failure to warn, strict liability, breach of warranty, conspiracy/concert of action, aiding and abetting, enterprise liability, market share or risk contribution liability, intentional tort, fraud and misrepresentation, violations of state consumer protection statutes, supplier negligence and similar claims.

The plaintiffs in these actions generally seek to impose on the defendants responsibility for lead paint abatement and health concerns associated with the use of lead-based paints, including damages for personal injury, contribution and/or indemnification for medical expenses, medical monitoring expenses and costs for educational programs. A number of cases are inactive or have been dismissed or withdrawn. Most of the remaining cases are in various pre-trial stages. Some are on appeal following dismissal or summary judgment rulings in favor of either the defendants or plaintiffs. In addition, various other cases are pending (in which NL is not a defendant) seeking recovery for injuries allegedly caused by lead pigment and lead-based paint. Although we are not a defendant in these cases, the outcome of these cases may have an impact on additional cases being filed against NL in the future.

We believe these actions are without merit, and intend to continue to deny all allegations of wrongdoing and liability and to defend against all actions vigorously. We have never settled any of these cases, nor have any final adverse judgments against us been entered. We have not accrued any amounts for pending lead pigment and lead-based paint litigation. We cannot reasonably estimate liability, if any, that may result. We cannot assure you that we will not incur liability in the future as a result of pending litigation due to the inherent uncertainties involved in court and jury rulings in pending and possible future cases. If future liabilities are incurred, it could have a material adverse effect on our consolidated financial statements, results of operations and liquidity.

In one of these lead pigment cases (State of Rhode Island v. Lead Industries Association), a trial before a Rhode Island state court jury began in September 2002 on the question of whether lead pigment in paint on Rhode Island buildings is a public nuisance. In October 2002, the trial judge declared a mistrial in the case when the jury was unable to reach a verdict on the question, with the jury reportedly deadlocked 4-2 in defendants' favor. In November 2005, the State of Rhode Island began a retrial of the case on the State's claims of public nuisance, indemnity and unjust enrichment. Following the State's presentation of its case, the trial court dismissed the State's claims of indemnity and unjust enrichment. The public nuisance claim was sent to the jury in February 2006, and the jury found that NL and two other defendants substantially contributed to the creation of a public nuisance as a result of the collective presence of lead pigments in paints and coatings on buildings in

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Rhode Island. The jury also found that NL and the two other defendants should be ordered to abate the public nuisance. Following the jury verdict, the trial court dismissed the State's claim for punitive damages. The scope of the abatement remedy will be determined by the judge. The extent, nature and cost of the abatement remedy are not currently known, and will be determined only following additional proceedings before the trial court. Various matters remain pending before the trial court, including NL's motion to dismiss. We intend to appeal any adverse judgment which the trial court may enter against us.

The Rhode Island case is unique because this is the first time that an adverse verdict in the lead pigment litigation has been entered against NL. NL believes there are a number of meritorious issues which can be appealed in this case; therefore, NL currently believes it is not probable it will ultimately be found liable in this matter. In addition, NL cannot reasonably estimate potential liability, if any, with respect to this and the other lead pigment litigation. However, legal proceedings are subject to inherent uncertainties, and we cannot assure you that any appeal would be successful. Therefore, it is reasonably possible NL could in the near term conclude it is probable NL has incurred some liability in this Rhode Island matter that would result in recognizing a loss contingency accrual. The potential liability could have a material adverse impact on net income for the interim or annual period during which the liability is recognized, and a material adverse impact on our financial condition and liquidity. Various other cases in which NL is a defendant are also pending in other jurisdictions, and new cases could be filed against NL, the resolution of which could also result in recognition of a loss contingency accrual that could have a material adverse impact on our net income for the interim or annual period during which such liability is recognized, and a material adverse impact on our financial condition and liquidity. We cannot currently reasonably estimate the potential impact on our results of operations, financial condition or liquidity related to these matters.

Environmental matters and litigation

General - Our operations are governed by various environmental laws and regulations. Certain of our businesses are and have been engaged in the handling, manufacture or use of substances or compounds that may be considered toxic or hazardous within the meaning of applicable environmental laws. As with other companies engaged in similar businesses, certain of our past and current operations and products have the potential to cause environmental or other damage. We have implemented and continue to implement various policies and programs in an effort to minimize these risks. Our policy is to maintain compliance with applicable environmental laws and regulations at all of our plants and to strive to improve our environmental performance. From time to time, we may be subject to environmental regulatory enforcement under U.S. and foreign statutes, the resolution of which typically involves the establishment of compliance programs. Future developments, such as stricter requirements of environmental laws and enforcement policies, could adversely affect our production, handling, use, storage, transportation, sale or disposal of such substances. We believe all of our plants are in substantial compliance with applicable environmental laws.

Certain properties and facilities used in our former businesses, including divested primary and secondary lead smelters and former mining locations of NL, are the subject of civil litigation, administrative proceedings or investigations arising under federal and state environmental laws. Additionally, in connection with past disposal practices, we have been named as a defendant, potentially responsible party ("PRP") or both, pursuant to the Comprehensive Environmental Response, Compensation and Liability Act, as amended by the Superfund Amendments and Reauthorization Act ("CERCLA"), and similar state laws in various governmental and private actions associated with waste disposal sites, mining locations, and facilities we or our predecessors currently or previously owned, operated or used, certain of which are on the U.S. EPA's

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Superfund National Priorities List or similar state lists. These proceedings seek cleanup costs, damages for personal injury or property damage and/or damages for injury to natural resources. Certain of these proceedings involve claims for substantial amounts. Although we may be jointly and severally liable for these costs, in most cases we are only one of a number of PRPs who may also be jointly and severally liable.

Environmental obligations are difficult to assess and estimate for numerous reasons including:

- o complexity and differing interpretations of governmental regulations,
- o number of PRPs and their ability or willingness to fund such allocation of costs,
- o financial capabilities of the PRPs and the allocation of costs among them,
- o solvency of other PRPs,
- o multiplicity of possible solutions; and
- o the years of investigatory, remedial and monitoring activity required.

In addition, the imposition of more stringent standards or requirements under environmental laws or regulations, new developments or changes respecting site cleanup costs or allocation of costs among PRPs, solvency of other PRPs, the results of future testing and analysis undertaken with respect to certain sites or a determination that we are potentially responsible for the release of hazardous substances at other sites, could cause our expenditures to exceed our current estimates. Because we may be jointly and severally liable for the total remediation cost at certain sites, the amount we are ultimately liable for may exceed our accruals due to, among other things, reallocation of costs among PRPs or the insolvency of one or more PRPs. We cannot assure you that actual costs will not exceed accrued amounts or the upper end of the range for sites for which estimates have been made, nor can we assure you that costs will not be incurred for sites where no estimate presently can be made. Further, additional environmental matters may arise in the future. If we were to incur any future liability, this could have a material adverse effect on our consolidated financial position, results of operations and liquidity.

We record liabilities related to environmental remediation obligations when estimated future expenditures are probable and reasonably estimable. Environmental accruals are adjusted as further information becomes available or circumstances change. Estimated future expenditures are generally not discounted to their present value due to the uncertainty of the timing of the pay out. We recognize recoveries of remediation costs from other parties, if any, when their receipt is deemed probable. At June 30, 2006, there were no receivables for recoveries.

We do not know and cannot estimate the exact time frame over which we will make payments for our accrued environmental costs. The timing of payments depends upon a number of factors including the timing of the actual remediation process; this in turn depends on factors outside of our control. At each balance sheet date, we estimate the amount of our accrued environmental costs we will pay within the next 12 months. We classify this estimate as a current liability, and we classify the remaining accrued environmental costs as a noncurrent liability on our Consolidated Balance Sheet.

Changes in the accrued environmental costs during the first six months of 2006 are as follows:

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Balance at the beginning of the period
Additions charged to expense, net
Payments, net

Balance at the end of the period

Amounts recognized in the balance sheet at the end of the period:
Current liability
Noncurrent liability

Total

NL - On a quarterly basis, NL evaluates the potential range of its liability at sites where it has been named as a PRP or defendant. At June 30, 2006, NL had accrued \$52.7 million for those environmental matters which NL believes are reasonably estimable. NL believes it is not possible to estimate the range of costs for certain sites. The upper end of the range of reasonably possible costs for sites for which NL believes it is currently possible to estimate costs is approximately \$78 million. NL has not discounted these estimates to present value.

At June 30, 2006, there are approximately 20 sites for which NL is unable to estimate a range of costs. For these sites, generally the investigation is in the early stages, and it is either unknown as to whether NL actually had any association with the site, or if NL had an association with the site, the nature of its responsibility, if any, for the contamination at the site and the extent of contamination. NL cannot estimate when enough information will become available to allow it to estimate a range of loss. The timing and availability of information on these sites is dependent on events outside the control of NL, such as when the party alleging liability provides information to NL. On certain previously inactive sites, NL has received general and special notices of liability from the EPA alleging that NL, along with other PRPs, is liable for past and future costs of remediating environmental contamination allegedly caused by former operations conducted at the sites. These notifications may assert that NL, along with other PRPs, is liable for past clean-up costs. These costs could be material to us if liability for the costs ultimately were determined against NL.

Tremont - Prior to 2005, Tremont, another of our wholly-owned subsidiaries, entered into a voluntary settlement agreement with the Arkansas Department of Environmental Quality and certain other PRPs pursuant to which Tremont and the other PRPs will undertake certain investigatory and interim remedial activities at a former mining site located in Hot Springs County, Arkansas. Tremont had entered into an agreement with Halliburton Energy Services, Inc., another PRP for this site that provides for, among other things, the interim sharing of remediation costs associated with the site pending a final allocation of costs and an agreed-upon procedure through arbitration to determine the final allocation of costs. On December 9, 2005, Halliburton and DII Industries, LLC, another PRP of this site, filed suit in the United States District Court for the Southern District of Texas, Houston Division, Case No. H-05-4160, against NL, Tremont and certain of its subsidiaries, M-I, L.L.C., Milwhite, Inc. and Georgia-Pacific Corporation seeking:

- o to recover response and remediation costs incurred at the site,
- o a declaration of the parties' liability for response and remediation costs incurred at the site,
- o a declaration of the parties' liability for response and remediation

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- o costs to be incurred in the future at the site; and
- o a declaration regarding the obligation of Tremont to indemnify Halliburton and DII for costs and expenses attributable to the site.

On December 27, 2005, a subsidiary of Tremont filed suit in the United States District Court for the Western District of Arkansas, Hot Springs Division, Case No. 05-6089, against Georgia-Pacific, seeking to recover response costs it has incurred and will incur at the site. Subsequently, plaintiffs in the Houston litigation agreed to stay that litigation by entering into an amendment with NL, Tremont and its affiliates to the arbitration agreement previously agreed upon for resolving the allocation of costs at the site. Tremont has also agreed with Georgia Pacific to stay the Arkansas litigation pending further developments in the Houston litigation, where the court recently agreed to stay the plaintiffs claims against Tremont and its subsidiaries, and denied Tremont's motions to dismiss and to stay the claims made by M-I, Milwhite and Georgia Pacific. Tremont has accrued for this site based upon the agreed-upon interim cost sharing allocation. Tremont has \$3.3 million accrued at June 30, 2006 which represents the probable and reasonably estimable costs to be incurred through 2008 with respect to the interim remediation measures. Tremont currently expects the nature and extent of any final remediation measures for this site will not be known until 2008. Tremont has not accrued costs for this site for any final remediation measures since no reasonable estimate can currently be made of the cost of any final remediation measures.

TIMET - At June 30, 2006, TIMET had accrued approximately \$2.2 million for environmental cleanup matters, principally related to their facility in Nevada. The upper end of the range of reasonably possible costs related to these matters, including the current accrual, is approximately \$4.4 million.

Other - We have also accrued approximately \$7.8 million at June 30, 2006 for other environmental cleanup matters related to us. This accrual is near the upper end of the range of our estimate of reasonably possible costs for such matters.

Other litigation

NL has been named as a defendant in various lawsuits in several jurisdictions, alleging personal injuries as a result of occupational exposure primarily to products manufactured by formerly-owned operations of NL containing asbestos, silica and/or mixed dust. Approximately 500 of these types of cases remain pending, involving a total of approximately 10,600 plaintiffs and their spouses. NL has not accrued any amounts for this litigation because of the uncertainty of liability and inability to reasonably estimate the liability, if any. To date, NL has not been adjudicated liable in any of these matters. Based on information available to NL, including:

- o facts concerning its historical operations,
- o the rate of new claims,
- o the number of claims from which NL has been dismissed; and
- o NL's prior experience in the defense of these matters

NL believes the range of reasonably possible outcomes of these matters will be consistent with its historical costs (which are not material), and NL does not expect any reasonably possible outcome would involve amounts that are material to NL. NL has and will continue to vigorously seek dismissal from each claim and/or a finding of no liability by NL in each case. In addition, from time to time, NL has received notices regarding asbestos or silica claims purporting to be brought against its former subsidiaries, including notices provided to insurers with which NL has entered into settlements extinguishing certain insurance policies. These insurers may seek indemnification from NL.

Murphy, et al. v. NL Industries, Inc., et al. (United States District

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Court, District of New Jersey, Case No. 2:06-cv-01535-WHW-SDW). In June 2006, the plaintiffs filed an amended complaint. In July 2006, defendants filed motions to disqualify plaintiffs' counsel, compel arbitration, transfer venue to the Northern District of Texas, dismiss the claims against the individual defendants for lack of personal jurisdiction and to dismiss the entire complaint.

For a discussion of other legal proceedings to which we are a party, refer to the consolidated financial statements included in our 2005 Annual Report and in our Quarterly Report on Form 10-Q for the quarter ended March 31, 2006.

In addition to the litigation described above, we and our affiliates are also involved in various other environmental, contractual, product liability, patent (or intellectual property), employment and other claims and disputes incidental to our present and former businesses. In certain cases, we have insurance coverage for these items, although we do not currently expect any additional material insurance coverage for our environmental claims.

We currently believe the disposition of all claims and disputes, individually or in the aggregate, should not have a material adverse effect on our consolidated financial position, results of operations and liquidity beyond the accruals already provided for.

Insurance coverage claims

For a complete discussion of certain litigation involving us and certain of our former insurance carriers, refer to the 2005 Annual Report and our Quarterly Report on Form 10-Q for the quarter ended March 31, 2006. Additional information regarding such litigation, or new litigation, is below.

NL Industries, Inc. v. OneBeacon America Insurance Company, et. al. (District Court for Dallas County, Texas, Case No. 05-11347). In June 2006, the federal court granted our motion to remand the action to Texas state court.

The issue of whether insurance coverage for defense costs or indemnity or both will be found to exist for NL's lead pigment litigation depends upon a variety of factors, and there can be no assurance that such insurance coverage will be available. NL has not considered any potential insurance recoveries for lead pigment or environmental litigation matters in determining related accruals.

Note 16 - Recent accounting pronouncements:

Inventory Costs - Statement of Financial Accounting Standards ("SFAS") No. 151, Inventory Costs, an amendment of ARB No. 43, Chapter 4, became effective for us for inventory costs incurred on or after January 1, 2006. SFAS No. 151 requires that the allocation of fixed production overhead costs to inventory be based on normal capacity of the production facilities, as defined by SFAS No. 151. SFAS No. 151 also clarifies the accounting for abnormal amounts of idle facility expense, freight handling costs and wasted material, requiring those items be recognized as current-period charges. Our existing production cost policies complied with the requirements of SFAS No. 151, therefore the adoption of SFAS No. 151 did not affect our Consolidated Financial Statements.

Stock Options - We adopted the fair value provisions of SFAS No. 123R, Share-Based Payment, on January 1, 2006 using the modified prospective application method. SFAS No. 123R, among other things, requires the cost of

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employee compensation paid with equity instruments to be measured based on the grant-date fair value. That cost is then recognized over the vesting period. Using the modified prospective method, we will apply the provisions of the standard to all new equity compensation granted after January 1, 2006 and any existing awards vesting after January 1, 2006. The number of non-vested equity awards issued by us or our subsidiaries as of December 31, 2005 is not material. Prior to the adoption of SFAS No. 123R we accounted for our equity compensation in accordance with APBO No. 25, Accounting for Stock Issued to Employees. Our subsidiary NL accounted for their equity awards under the variable accounting method whereby the equity awards were revalued based on the current trading price at each balance sheet date. We now account for these awards using the liability method under SFAS No. 123R, which is substantially identical to the variable accounting method we previously used. We recorded net compensation income for stock-based employee compensation of approximately \$1.4 million and \$1.3 million in the second quarter and first six months of 2005, respectively, and we recorded net compensation income of approximately \$400,000 in the first six months of 2006. We recorded no compensation income or expense in the second quarter of 2006 for stock-based employee compensation. If we or our subsidiaries grant a significant number of equity awards or modify, repurchase or cancel existing equity awards in the future, the amount of equity compensation expense in our Consolidated Financial Statements could be material.

Effective January 1, 2006, SFAS No. 123R requires the cash income tax benefit resulting from the exercise of stock options in excess of the cumulative income tax benefit previously recognized for GAAP financial reporting purposes (which for us did not represent a significant amount in the first six months of 2006) to be reflected as a component of cash flows from financing activities in our Consolidated Financial Statements. SFAS No. 123R also requires certain expanded disclosures regarding equity compensation, and we provided these expanded disclosures in our 2005 Annual Report.

Uncertain tax positions - In the second quarter of 2006 the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. ("FIN") 48, Accounting for Uncertain Tax Positions, which will become effective for us on January 1, 2007. FIN No. 48 clarifies when and how much of a benefit we can recognize in our Consolidated Financial Statements for certain positions taken in our income tax returns under SFAS No. 109, Accounting for Income Taxes, and enhances the disclosure requirements for our income tax policies and reserves. Among other things, FIN No. 48 will prohibit us from recognizing the benefits of a tax position unless we believe it is more-likely-than-not our position will prevail with the applicable tax authorities and limits the amount of the benefit to the largest amount for which we believe the likelihood of realization is greater than 50%. FIN No. 48 also requires companies to accrue penalties and interest on the difference between tax positions taken on their tax returns and the amount of benefit recognized for financial reporting purposes under the new standard. Our current income tax accounting policies comply with this aspect of the new standard. We will also be required to reclassify any reserves we have for uncertain tax positions from deferred income tax liabilities, where they are currently recognized, to a separate current or noncurrent liability, depending on the nature of the tax position. We are currently evaluating the impact of FIN No. 48 on our Consolidated Financial Statements.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

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RESULTS OF OPERATIONS

Business Overview

We are primarily a holding company. We operate through our wholly-owned and majority-owned subsidiaries, including NL Industries, Inc., Kronos Worldwide, Inc., CompX International, Inc., Tremont LLC and Waste Control Specialists LLC. We also own a non-controlling interest in Titanium Metals Corporation ("TIMET"). Kronos (NYSE: KRO), NL (NYSE: NL), CompX (NYSE: CIX) and TIMET (NYSE: TIE) each file periodic reports with the Securities and Exchange Commission ("SEC").

We have three consolidated operating segments:

- o Chemicals - Our chemicals segment is operated through our majority ownership of Kronos. Kronos is a leading global producer and marketer of value-added titanium dioxide pigments ("TiO2"). TiO2 is used for a variety of manufacturing applications, including plastics, paints, paper and other industrial products.
- o Component Products - We operate in the component products industry through our majority ownership of CompX. CompX is a leading manufacturer of precision ball bearing slides, security products and ergonomic computer support systems used in office furniture, transportation, tool storage and a variety of other industries. CompX has recently entered the performance marine components industry through the acquisition of two performance marine manufacturers.
- o Waste Management - WCS is our wholly-owned subsidiary which owns and operates a West Texas facility for the processing, treatment, storage and disposal of hazardous, toxic and certain types of low-level radioactive waste. WCS is in the process of obtaining regulatory authorization to expand its low-level and mixed-level radioactive waste handling capabilities.

In addition, we account for our 35% non-controlling interest in TIMET by the equity method. TIMET is a leading global producer of titanium sponge, melted products and milled products. Titanium is used for a variety of commercial, aerospace, military, medical and other emerging markets. TIMET is also the only titanium producer with major production facilities in both of the world's principal titanium markets: the U.S. and Europe.

General

This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Statements in this Quarterly Report on Form 10-Q that are not historical in nature are forward-looking in nature about our future that are not statements of historical fact. Statements in this report including, but not limited to, statements found in Item 2 - "Management's Discussion and Analysis of Financial Condition and Results of Operations," are forward-looking statements that represent our beliefs and assumptions based on currently available information. In some cases you can identify these forward-looking statements by the use of words such as "believes," "intends," "may," "should," "could," "anticipates," "expected" or comparable terminology, or by discussions of strategies or trends. Although we believe the expectations reflected in forward-looking statements are reasonable, we do not know if these expectations will be correct. Forward-looking statements by their nature involve substantial risks and uncertainties that could significantly impact expected results. Actual future results could differ materially from those predicted. While it is not possible to identify all factors, we continue to face many risks and uncertainties. Among the factors that could cause our actual future results to differ materially from those

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described herein are the risks and uncertainties discussed in this Quarterly Report and those described from time to time in our other filings with the SEC including, but not limited to, the following:

- o Future supply and demand for our products,
- o The extent of the dependence of certain of our businesses on certain market sectors (such as the dependence of TIMET's titanium metals business on the commercial aerospace industry),
- o The cyclical nature of certain of our businesses (such as Kronos' TiO₂ operations and TIMET's titanium metals operations),
- o The impact of certain long-term contracts on certain of our businesses (such as the impact of TIMET's long-term contracts with certain of its customers and such customers' performance thereunder and the impact of TIMET's long-term contracts with certain of its vendors on its ability to reduce or increase supply or achieve lower costs),
- o Customer inventory levels (such as the extent to which Kronos' customers may, from time to time, accelerate purchases of TiO₂ in advance of anticipated price increases or defer purchases of TiO₂ in advance of anticipated price decreases, or the relationship between inventory levels of TIMET's customers and such customers' current inventory requirements and the impact of such relationship on their purchases from TIMET),
- o Changes in our raw material and other operating costs (such as energy costs),
- o The possibility of labor disruptions,
- o General global economic and political conditions (such as changes in the level of gross domestic product in various regions of the world and the impact of such changes on demand for, among other things, TiO₂),
- o Competitive products and substitute products,
- o Possible disruption of our business or increases in the cost of doing business resulting from terrorist activities or global conflicts,
- o Customer and competitor strategies,
- o The impact of pricing and production decisions,
- o Competitive technology positions,
- o The introduction of trade barriers,
- o Fluctuations in currency exchange rates (such as changes in the exchange rate between the U.S. dollar and each of the euro, the Norwegian kroner and the Canadian dollar),
- o Operating interruptions (including, but not limited to, labor disputes, leaks, natural disasters, fires, explosions, unscheduled or unplanned downtime and transportation interruptions),
- o The timing and amounts of insurance recoveries,
- o Our ability to renew or refinance credit facilities,
- o The extent to which our subsidiaries were to become unable to pay us dividends,
- o Uncertainties associated with new product development (such as TIMET's ability to develop new end-uses for its titanium products),
- o The ultimate outcome of income tax audits, tax settlement initiatives or other tax matters,
- o The ultimate ability to utilize income tax attributes, the benefit of which has been recognized under the "more likely than not" recognition criteria (such as Kronos' ability to utilize its German net operating loss carryforwards),
- o Environmental matters (such as those requiring compliance with emission and discharge standards for existing and new facilities, or new developments regarding environmental remediation at sites related to our former operations),
- o Government laws and regulations and possible changes therein (such as changes in government regulations which might impose various obligations on present and former manufacturers of lead pigment and lead-based paint, including NL, with respect to asserted health

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- o concerns associated with the use of such products),
- o The ultimate resolution of pending litigation (such as NL's lead pigment litigation and litigation surrounding environmental matters of NL and Tremont), and
- o Possible future litigation.

Should one or more of these risks materialize (or the consequences of such development worsen), or should the underlying assumptions prove incorrect, actual results could differ materially from those currently forecasted or expected. We disclaim any intention or obligation to update or revise any forward-looking statement whether as a result of changes in information, future events or otherwise.

Net Income Overview

Quarter Ended June 30, 2005 Compared to the Quarter Ended June 30, 2006 -

We reported income from continuing operations of \$18.3 million, or \$.16 per diluted share, in the second quarter of 2006 compared to income of \$28.3 million, or \$.24 per diluted share, in the second quarter of 2005. Our diluted earnings per share declined from 2005 to 2006 due primarily to the net effects of:

- o lower chemicals operating income at Kronos in 2006,
- o higher component products operating income at CompX in 2006,
- o certain securities transaction gains realized in 2005,
- o a charge in 2006 from the redemption of our 8.875% Senior Secured Notes,
- o certain income tax benefits and another non-operating income item recognized by TIMET in 2005,
- o higher operating income for TIMET in 2006, and
- o certain income tax benefits recognized by Kronos in 2006.

Our income from continuing operations in 2005 includes (net of income taxes and minority interest): o a gain from the sale of our passive interest in a Norwegian smelting operation of \$.02 per diluted share, o income related to TIMET's sale of certain real property adjacent to its Nevada operations of \$.02 per diluted share, and o income related to certain income tax benefits recognized by TIMET of \$.01 per diluted share.

Our income from continuing operations in 2006 includes (net of income taxes and minority interest):

- o a charge related to the redemption of our 8.875% Senior Secured Notes of \$.09 per diluted share, and
- o an aggregate income tax benefit of \$.07 per diluted share associated with Kronos' operations related to the withdrawal of certain income tax assessments previously made by the Belgian and Norwegian tax authorities, the favorable resolution of certain income tax issues related to our German and Belgian operations and the enactment of a reduction in Canadian federal income tax rates.

These amounts are more fully discussed in this "Management's Discussion and Analysis of Financial Condition and Results of Operations - Results of Operations" or in the 2005 Annual Report.

We currently believe net income for the full year 2006 will be lower than 2005 primarily due to lower expected chemicals operating income.

Six Months Ended June 30, 2005 Compared to the Six Months Ended June 30,

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2006 -

We reported income from continuing operations of \$41.2 million, or \$.35 per diluted share, in the first six months of 2006 compared to income of \$53.4 million, or \$.44 per diluted share, in the first six months of 2005. Our diluted earnings per share declined from 2005 to 2006 due primarily to the net effects of:

- o lower chemicals operating income at Kronos in 2006,
- o higher component products operating income at CompX in 2006,
- o certain securities transaction gains realized in 2005,
- o a charge in 2006 from the redemption of our 8.875% Senior Secured Notes,
- o certain income tax benefits and another non-operating income item recognized by TIMET in 2005,
- o higher operating income for TIMET in 2006, and
- o certain income tax benefits recognized by Kronos in 2006.

Our income from continuing operations in 2005 includes (net of income taxes and minority interest): o gains from NL's sales of shares of Kronos common stock of \$.05 per diluted share, o a gain from the sale of our passive interest in a Norwegian smelting operation of \$.02 per diluted share, o income related to TIMET's sale of certain real property adjacent to its Nevada operations of \$.02 per diluted share, and o income related to certain income tax benefits recognized by TIMET of \$.08 per diluted share.

Our income from continuing operations in 2006 includes (net of income taxes and minority interest):

- o a charge related to the redemption of our 8.875% Senior Secured Notes of \$.09 per diluted share,
- o an aggregate income tax benefit of \$.07 per diluted share associated with Kronos' operations related to the withdrawal of certain income tax assessments previously made by the Belgian and Norwegian tax authorities, the favorable resolution of certain income tax issues related to our German and Belgian operations and the enactment of a reduction in Canadian federal income tax rates, and
- o income of \$.01 per diluted share related to certain insurance recoveries recognized by NL.

Segment Operating Results - 2005 Compared to 2006 -

Chemicals -

We consider TiO₂ to be a "quality of life" product, with demand affected by gross domestic product (or "GDP") in various regions of the world. Over the long-term, we expect that demand for TiO₂ will grow by 2% to 3% per year, consistent with our expectations for the long-term growth in GDP. However, even if we and our competitors maintain consistent shares of the worldwide market, demand for TiO₂ in any interim or annual period may not change in the same proportion as the change in GDP, in part due to relative changes in the TiO₂ inventory levels of our customers. We believe that our customers' inventory levels are partly influenced by their expectation for future changes in market TiO₂ selling prices.

The factors having the most impact on our reported operating results are

- o The level of our TiO₂ average selling prices,
- o Foreign currency exchange rates (particularly the exchange rate for the U.S. dollar relative to the euro and the Canadian dollar),
- o The level of our TiO₂ sales and production volumes, and
- o Manufacturing costs, particularly maintenance and energy-related

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expenses.

The key performance indicators for our Chemicals Segment are our TiO2 average selling prices, and our TiO2 sales and production volumes.

	Three months ended June 30,			Six months ended	
	2005	2006	% Change	2005	2006
	(Dollars in millions)				
Net sales	\$311.7	\$345.1	+11%	\$603.6	\$651.5
Cost of sales	220.8	266.8	+21%	432.4	488.2
Gross margin	\$ 90.9	\$ 78.3	-14%	\$171.2	\$163.3
Operating income	\$ 55.1	\$ 34.3	-38%	\$ 98.7	\$ 58.4
Percent of net sales:					
Cost of goods sold	71%	77%		72%	75%
Gross margin	29%	23%		28%	25%
Operating income	18%	10%		16%	9%
TiO2 operating statistics:					
Sales volumes*	122	139	+14%	237	271
Production volumes*	127	130	+2%	249	252
Percent change in net sales:					
Product pricing			-1%		
Sales volumes			+14%		
TiO2 product mix			-1%		
Foreign currency exchange rates			-1%		

			+11%		

* Thousands of metric tons

Net sales - Our Chemicals sales increased \$33.4 million (11%) in the second quarter of 2006 compared to the second quarter of 2005 due primarily to the net effects of (i) a 14% increase in TiO2 sales volumes, (ii) a 1% decrease in average TiO2 selling prices and (iii) the unfavorable effect of fluctuations in foreign currency exchange rates, which decreased sales by approximately \$4 million, or 1%. Chemicals sales increased \$45.9 million (8%) in the first six months of 2006 compared to the first six months of 2005 due primarily to an 11% increase in TiO2 sales volumes, somewhat offset by the unfavorable effect of changes in currency exchange rates, which decreased Chemicals sales by approximately \$19 million, or 3%. We expect our TiO2 average selling prices will remain reasonably stable in the second half of 2006 as compared to the second quarter of 2006.

The increase in our TiO2 sales volumes in 2006 was due primarily to higher sales volumes in the United States, Europe and in export markets, which were somewhat offset by lower sales volumes in Canada. Kronos' sales volumes in the first half of 2006 were a new record for Kronos. We believe Chemicals sales

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volumes in Canada have decreased as our customers demand has been affected by the effects of the strengthened Canadian dollar. We expect demand for TiO₂ will continue to remain high for the remainder of the year.

Cost of sales - Our Chemicals cost of sales increased in 2006 due primarily to the impact of higher sales volumes and higher operating costs. Cost