JOHNSON CONTROLS INC
Form 10-Q
January 31, 2005

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

FORM 10-Q

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

For the quarterly period ended December 31, 2004

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 1-5097

JOHNSON CONTROLS, INC.

(Exact name of registrant as specified in its charter)

Wisconsin (State of Incorporation)	39-0380010 (I.R.S. Employer Identification No.)

5757 North Green Bay Avenue, P.O. Box 591, Milwaukee, WI 53201
(Address of principal executive office)

Registrant s telephone number, including area code: (414) 524-1200

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 þ No o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes þ No o

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Class	Outstanding at December 31, 2004

Common Stock $.04 1/6 Par Value	191,174,330

JOHNSON CONTROLS, INC.

FORM 10-Q

December 31, 2004

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PART I. - FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

JOHNSON CONTROLS, INC.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

(in millions; unaudited)

	December 31, 2004	September 30, 2004	December 31, 2003
ASSETS			
Cash and cash equivalents	$ 240.7	$ 169.5	$ 302.6
Accounts receivable - net	3,994.7	4,073.6	3,410.7
Costs and earnings in excess of billings on uncompleted contracts	362.0	328.6	318.7
Inventories	949.8	887.2	810.7
Assets of discontinued operations	426.4	394.4	367.0
Other current assets	882.5	780.0	790.5
Current assets	6,856.1	6,633.3	6,000.2
Property, plant and equipment - net	3,614.1	3,473.3	3,079.5
Goodwill - net	3,756.3	3,609.1	3,143.7
Other intangible assets - net	299.1	291.0	267.8
Investments in partially-owned affiliates	325.3	314.9	425.9
Other noncurrent assets	825.7	769.2	753.8
Total assets	$ 15,676.6	$ 15,090.8	$ 13,670.9
LIABILITIES AND SHAREHOLDERS EQUITY			
Short-term debt	$ 901.9	$ 813.3	$ 717.6
Current portion of long-term debt	217.5	226.8	130.9
Accounts payable	3,528.6	3,664.4	3,181.1
Accrued compensation and benefits	603.5	639.2	472.4
Accrued income taxes	20.4	47.4	100.2
Billings in excess of costs and earnings on uncompleted contracts	218.8	197.2	204.4
Liabilities of discontinued operations	119.8	128.1	97.0
Other current liabilities	1,012.9	885.2	827.9
Current liabilities	6,623.4	6,601.6	5,731.5
Long-term debt	1,668.5	1,630.6	1,830.6
Postretirement health and other benefits	163.6	164.1	167.1
Minority interests in equity of subsidiaries	294.8	268.7	229.5
Other noncurrent liabilities	1,344.7	1,219.5	1,130.6

Shareholders equity	5,581.6	5,206.3	4,581.6
Total liabilities and shareholders equity	$ 15,676.6	$ 15,090.8	$ 13,670.9

The accompanying notes are an integral part of the financial statements.

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JOHNSON CONTROLS, INC.

CONSOLIDATED STATEMENT OF INCOME
(in millions, except per share data; unaudited)

	Three Months Ended December 31, 2004	Three Months Ended December 31, 2003
Net sales		
Products and systems*	$ 6,016.4	$ 5,428.8
Services*	959.1	864.1
	6,975.5	6,292.9
Cost of sales		
Products and systems	5,327.6	4,726.6
Services	805.1	720.7
	6,132.7	5,447.3
Gross profit	842.8	845.6
Selling, general and administrative expenses	597.4	592.1
Operating income	245.4	253.5
Interest income	4.4	1.9
Interest expense	(30.9)	(27.2)
Equity income	15.8	17.8
Miscellaneous - net	(4.6)	(24.6)
Other income (expense)	(15.3)	(32.1)
Income from continuing operations before income taxes and minority interests	230.1	221.4
Provision for income taxes	48.6	46.7
Minority interests in net earnings of subsidiaries	21.0	15.5
Income from continuing operations	160.5	159.2
Income from discontinued operations, net of income taxes	7.9	5.3
Net income	$ 168.4	$ 164.5

Earnings available for common shareholders	$	168.4	$	162.7
Earnings per share from continuing operations				
Basic	$	0.84	$	0.87
Diluted	$	0.83	$	0.83
Earnings per share				
Basic	$	0.88	$	0.90
Diluted	$	0.87	$	0.86

* Products and systems consist of Automotive Group products and systems and Controls Group installed systems. Services are Controls Group technical and facility management services.

The accompanying notes are an integral part of the financial statements.

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JOHNSON CONTROLS, INC.

CONSOLIDATED STATEMENT OF CASH FLOWS
(in millions; unaudited)

	Three Months Ended December 31, 2004	Three Months Ended December 31, 2003
Operating Activities		
Income from continuing operations	$ 160.5	$ 159.2
Adjustments to reconcile income from continuing operations to cash provided by operating activities		
Depreciation	158.7	140.1
Amortization of intangibles	5.8	4.9
Equity in earnings of partially-owned affiliates, net of dividends received	(15.4)	(4.4)
Minority interests in net earnings of subsidiaries	21.0	15.5
Deferred income taxes	(0.4)	7.2
Other	(1.6)	2.7
Changes in working capital, excluding acquisition of businesses		
Receivables	263.0	176.7
Inventories	(14.3)	10.7
Other current assets	(41.4)	30.3
Accounts payable and accrued liabilities	(327.6)	(384.7)
Accrued income taxes	16.8	43.8
Billings in excess of costs and earnings on uncompleted contracts	15.1	13.6
Cash provided by operating activities of continuing operations	240.2	215.6
Cash (used) provided by operating activities of discontinued operations	(5.7)	31.4
Cash provided by operating activities	234.5	247.0
Investing Activities		
Capital expenditures	(143.6)	(197.6)
Sale of property, plant and equipment	4.2	8.9
Acquisition of businesses, net of cash acquired	(33.1)	(36.6)
Recoverable customer engineering expenditures	(8.6)	(49.1)
Changes in long-term investments	(2.0)	5.2
Net investing activities of discontinued operations	(3.0)	(6.0)
Cash used by investing activities	(186.1)	(275.2)
Financing Activities		
Increase in short-term debt - net	79.8	592.7
Increase in long-term debt	3.4	49.9

Repayment of long-term debt	(76.7)	(423.9)
Payment of cash dividends	(3.6)	(5.4)
Other	11.2	6.8
Net financing activities of discontinued operations	8.7	(25.4)
Cash provided by financing activities	22.8	194.7
Increase in cash and cash equivalents	$ 71.2	$ 166.5

The accompanying notes are an integral part of the financial statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. Financial Statements

In the opinion of the Company, the accompanying unaudited condensed consolidated financial statements contain all adjustments (consisting of only normal recurring accruals) necessary to present fairly the financial position, results of operations and cash flows for the periods presented. These condensed financial statements should be read in conjunction with the audited financial statements and notes thereto contained in the Company s Annual Report to Shareholders for the year ended September 30, 2004. The September 30, 2004 Consolidated Statement of Financial Position is derived from the audited financial statements, adjusted for discontinued operations (See Note 3). The results of operations for the three-month period ended December 31, 2004 are not necessarily indicative of the results which may be expected for the Company s 2005 fiscal year because of seasonal and other factors. Certain prior period amounts have been reclassified to conform to the current year s presentation.

2. Inventories

Inventories are valued at the lower of cost or market. Cost is determined using the last-in, first-out (LIFO) method for most inventories at domestic locations. The cost of other inventories is determined on the first-in, first-out (FIFO) method. Finished goods and work-in-process inventories include material, labor and manufacturing overhead costs. Inventories were comprised of the following:

(in millions)	December 31, 2004	September 30, 2004	December 31, 2003
Raw materials and supplies	$ 498.5	$ 485.2	$ 459.0
Work-in-process	138.1	137.0	108.7
Finished goods	341.1	292.8	269.7
FIFO inventories	977.7	915.0	837.4
LIFO reserve	(27.9)	(27.8)	(26.7)
Inventories	$ 949.8	$ 887.2	$ 810.7

3. Discontinued Operations

On January 10, 2005, the Company announced that it intends to sell its engine electronics business to Valeo for approximately 330 million, or approximately $437 million. The transaction, which is subject to regulatory approvals, is expected to be completed in the second quarter of fiscal 2005. This non-core business, which was a part of the Sagem SA automotive electronics business that was acquired in fiscal 2002, is reported as discontinued operations in the Consolidated Financial Statements. Under the requirements of Statement of Financial Accounting Standards (SFAS) No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, the income statement components of the discontinued operations will be aggregated and presented on a single line in the Consolidated Statement of Income through the date of sale.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

The following table summarizes the revenues and expenses of the discontinued operations:

	Three Months Ended December 31,	
(in millions)	2004	2003
Net sales	$ 118.8	$ 91.2
Cost of sales	99.8	75.5
Gross profit	19.0	15.7
Selling, general and administrative expenses	6.8	7.4
Operating income	12.2	8.3
Provision for income taxes	4.3	3.0
Net income	$ 7.9	$ 5.3
Earnings per share of discontinued operations		
Basic	$ 0.04	$ 0.03
Diluted	$ 0.04	$ 0.03

The Consolidated Statement of Financial Position at December 31, 2004 includes assets of discontinued operations of $426.4 million, consisting of goodwill ($157.2 million), accounts receivable ($100.0 million), property, plant and equipment net ($60.7 million), other intangible assets net ($59.5 million) and other miscellaneous assets ($49.0 million). Liabilities of discontinued operations at December 31, 2004 totaled $119.8 million, consisting of accounts payable ($89.6 million), accrued compensation ($23.6 million) and other miscellaneous liabilities ($6.6 million).

4. Product Warranties

The Company provides warranties to certain of its customers depending upon the specific product and terms of the customer purchase agreement. Most of the Company s product warranties are customer specific. A typical warranty program requires replacement of defective products within a specified time period from the date of sale. The Company records an estimate for future warranty-related costs based on actual historical return rates. Based on analysis of return rates and other factors, the warranty provisions are adjusted as necessary. While warranty costs have historically been within calculated estimates, it is possible that future warranty costs could exceed those estimates. The Company s product warranty liability is included in Other current liabilities in the Consolidated Statement of Financial Position.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

The changes in the carrying amount of total product warranty liability for the three-month period ended December 31, 2004 were as follows:

(in millions)	
Balance as of September 30, 2004	$ 69.8
Accruals for warranties issued during the period	10.2
Accruals related to pre-existing warranties (including changes in estimates)	(0.6)
Settlements made (in cash or in kind) during the period	(10.9)
Currency translation	2.6
Balance as of December 31, 2004	$ 71.1

5. Stock-Based Compensation Stock Options

Effective October 1, 2002, the Company voluntarily adopted the fair value recognition provisions of SFAS No. 123, Accounting for Stock-Based Compensation and adopted the disclosure requirements of SFAS No. 148, Accounting for Stock-Based Compensation-Transition and Disclosure an amendment of FAS 123. In accordance with SFAS No. 148, the Company has adopted the fair value recognition provisions on a prospective basis and, accordingly, the expense recognized in the three-month period ended December 31, 2004 represents a pro rata portion of the fiscal 2005, 2004 and 2003 grants which are earned over a three-year vesting period.

The following table illustrates the pro forma effect on net income and earnings per share as if the fair value based method had been applied to all outstanding and unvested awards in each period:

	Three Months Ended December 31,	
(in millions)	2004	2003
Net income, as reported	$ 168.4	$ 164.5
Add: Stock-based employee compensation expense included in reported net income, net of related tax effects	3.4	3.6
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(4.7)	(5.5)
Pro forma net income	$ 167.1	$ 162.6
Earnings per share		
Basic - as reported	$ 0.88	$ 0.90
Basic - pro forma	$ 0.88	$ 0.89
Diluted - as reported	$ 0.87	$ 0.86
Diluted - pro forma	$ 0.86	$ 0.85

During December 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 123R, Share-Based Payment (SFAS 123R), which requires companies to measure and recognize compensation expense for all stock-based payments at fair value. Stock-based payments include stock option grants and certain transactions

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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under other Company stock plans. The Company grants options to purchase common stock to some of its employees and directors under various plans at prices equal to the market value of the stock on the dates the options were granted. SFAS 123R is effective for all interim or annual periods beginning after June 15, 2005. The Company is currently evaluating the impact that the adoption of SFAS 123R will have on its consolidated financial position, results of operations and cash flows.

6. Guarantees

The Company has guaranteed the residual value related to the Company aircraft accounted for as synthetic leases. The guarantees extend through the lease maturity dates of September 2006. In the event the Company exercised its option not to purchase the aircraft for the remaining obligations at the scheduled maturity of the leases, the Company has guaranteed the majority of the residual values, not to exceed $53 million in aggregate. The Company has recorded a liability of approximately $3 million within Other noncurrent liabilities and a corresponding amount within Other noncurrent assets in the Consolidated Statement of Financial Position relating to the Company s obligation under the guarantees. These amounts are being amortized over the life of the guarantees.

7. Earnings Per Share

The following table reconciles the numerators and denominators used to calculate basic and diluted earnings per share:

(in millions)	Three Months Ended December 31, 2004	2003
Income Available to Common Shareholders		
Income from continuing operations	$ 160.5	$ 159.2
Preferred stock dividends, net of tax benefit		(1.8)
Basic income available to common shareholders	$ 160.5	$ 157.4
Income from continuing operations	$ 160.5	$ 159.2
Effect of dilutive securities:		
Compensation expense, net of tax benefit, arising from assumed conversion of preferred stock		(0.1)
Diluted income available to common shareholders	$ 160.5	$ 159.1
Weighted Average Shares Outstanding		
Basic weighted average shares outstanding	190.7	181.0

Effect of dilutive securities:		
Stock options	2.9	3.3
Convertible preferred stock		7.5
Diluted weighted average shares outstanding	193.6	191.8
Antidilutive Securities		
Options to purchase common shares	0.4	0.1

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

8. Goodwill and Other Intangible Assets

The changes in the carrying amount of goodwill for the nine-month period ended September 30, 2004 and the three-month period ended December 31, 2004 were as follows:

(in millions)	Automotive Group	Controls Group	Total
Balance as of December 31, 2003	$ 2,690.4	$ 453.3	$ 3,143.7
Goodwill from business acquisitions	458.0		458.0
Currency translation	(5.9)	13.3	7.4
Other	1.9	(1.9)	
Balance as of September 30, 2004	3,144.4	464.7	3,609.1
Goodwill from business acquisitions		9.0	9.0
Currency translation	125.8	14.7	140.5
Other	(2.3)		(2.3)
Balance as of December 31, 2004	$ 3,267.9	$ 488.4	$ 3,756.3

The Company s other intangible assets, primarily from business acquisitions, are valued based on independent appraisals and consisted of: