SPS TECHNOLOGIES INC
Form 10-Q
November 15, 2002

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

FORM 10-Q

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

For the quarter ended September 30, 2002
Commission file number 1-4416

SPS TECHNOLOGIES, INC.

(Exact name of Registrant as specified in its Charter)

PENNSYLVANIA (State of incorporation) Two Pitcairn Place, Suite 200	23-1116110 (I.R.S. Employer Identification No.)
165 Township Line Road Jenkintown, Pennsylvania (Address of principal executive offices)	19046 (Zip Code)

(215) 517-2000
(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

The number of shares of Registrant's Common Stock outstanding on November 6, 2002 was 13,096,099.

SPS TECHNOLOGIES, INC. AND SUBSIDIARIES

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SPS TECHNOLOGIES, INC. AND SUBSIDIARIES
STATEMENTS OF CONSOLIDATED OPERATIONS
(Unaudited-Thousands of dollars, except share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2002	2001	2002	2001
Net sales	$205,125	$231,824	$628,783	$710,366
Cost of goods sold	170,275	188,821	520,407	568,069
Gross profit	34,850	43,003	108,376	142,297
Selling, general and administrative expense	24,534	25,577	75,466	80,141
Restructurings and Impairments	13,600	-	14,500	9,100
Operating earnings	(3,284)	17,426	18,410	53,056
Other income (expense):				
Interest income	201	107	619	500
Interest expense	(4,569)	(5,080)	(13,841)	(15,314)
Other, net	(1,094)	(183)	(1,324)	(252)
	(5,462)	(5,156)	(14,546)	(15,066)
Earnings (loss) before income taxes	(8,746)	12,270	3,864	37,990
Provision (benefit) for income taxes	(2,436)	3,910	1,494	12,200
Net earnings (loss)	$ (6,310)	$ 8,360	$ 2,370	$ 25,790
Earnings (loss) per common share:				
Basic	$ (0.48)	$ 0.64	$ 0.18	$ 1.99

Diluted	$ (0.48)	$ 0.63	$ 0.18	$ 1.95

See accompanying notes to condensed consolidated financial statements.

SPS TECHNOLOGIES, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Unaudited - Thousands of dollars)

	September 30, 2002	December 31, 2001
Assets		
Current assets		
Cash and cash equivalents	$ 35,036	$ 59,948
Accounts and notes receivable, less allowance for doubtful receivables of $4,893 (2001 - $4,880)	139,503	129,663
Inventories	164,898	175,151
Deferred income taxes	21,533	20,170
Prepaid expenses and other	6,881	8,346
Total current assets	367,851	393,278
Property, plant and equipment, net of accumulated depreciation of $180,000 (2001 - $167,976)	220,841	226,060
Intangible assets, net of amortization	2,905	3,342
Goodwill	209,150	206,572
Other assets	24,100	21,527
Total assets	$ 824,847	$ 850,779

See accompanying notes to condensed consolidated financial statements.

SPS TECHNOLOGIES, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Unaudited - Thousands of dollars, except share data)

	September 30, 2002	December 31, 2001
Liabilities and shareholders' equity		
Current liabilities		
Notes payable and current portion of long-term debt	$ 11,434	$ 20,096
Accounts payable	72,553	77,735
Accrued expenses	69,816	71,526
Income taxes payable	138	605
Total current liabilities	153,941	169,962
Deferred income taxes	27,281	26,370
Long-term debt	214,075	243,078
Retirement obligations and other long-term liabilities	61,021	58,684
Commitments and contingencies (note 9)		
Shareholders' equity		
Preferred stock, par value $1 per share, authorized 400,000 shares, issued none		
Common stock, par value $0.50 per share, authorized 60,000,000 shares, issued 14,473,559 shares (14,396,924 shares in 2001)	7,237	7,198
Additional paid-in capital	127,724	125,949
Common stock in treasury, at cost, 1,309,406 shares (1,286,374 shares in 2001)	(26,370)	(25,433)

Retained earnings	297,500	295,130
Accumulated other comprehensive income (loss)		
Minimum pension liability	(16,612)	(16,212)
Cumulative translation adjustments	(18,682)	(31,770)
Fair value of derivative adjustments	(2,268)	(2,177)
Total shareholders' equity	368,529	352,685
Total liabilities and shareholders' equity	$ 824,847	$ 850,779

See accompanying notes to condensed consolidated financial statements.

SPS TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED STATEMENTS OF CONSOLIDATED CASH FLOWS
(Unaudited-Thousands of dollars)

	Nine Months Ended September 30,	
	2002	2001
Net cash provided by operating activities (including depreciation and amortization of $22,735 in 2002 and $29,295 in 2001)	$ 28,516	$ 35,463
Cash flows provided by (used in) investing activities		
Additions to property, plant and equipment	(17,392)	(30,688)
Proceeds from sale of property, plant and equipment	1,725	327

Acquisitions of businesses, net of cash acquired	-	(21,712)
Net cash used in investing activities	(15,667)	(52,073)
Cash flows provided by (used in) financing activities		
Proceeds from borrowings	77,030	60,424
Reduction of borrowings	(115,173)	(51,937)
Proceeds from exercise of stock options	95	678
Net cash provided by (used in) financing activities	(38,048)	9,165
Effect of exchange rate changes on cash	287	(190)
Net increase (decrease) in cash and cash equivalents	(24,912)	(7,635)
Cash and cash equivalents at beginning of period	59,948	31,933
Cash and cash equivalents at end of period	$ 35,036	$ 24,298
Significant noncash investing and financing activities:		
Issuance of treasury shares for businesses acquired	$ -	$ 6,975
Debt assumed with businesses acquired	$ -	$ 3,616
Acquisition of treasury shares for stock options exercised	$ 933	$ 2,541

See accompanying notes to condensed consolidated financial statements.

SPS TECHNOLOGIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited - Thousands of dollars)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2002	2001	2002	2001
Net earnings (loss)	$(6,310)	$ 8,360	$ 2,370	$25,790
Other comprehensive income (expense), net of tax:				
Changes in minimum pension liability	100	-	(400)	-
Foreign currency translation adjustments	7,492	3,085	13,088	(3,899)
Derivatives:				
Changes in fair values	822	(34)	809	(3,126)
Reclassification to net earnings adjustment	(900)	-	(900)	-
Cumulative effect of accounting change, SFAS No. 133	-	-	-	250
Total comprehensive income	$ 1,204	$11,411	$14,967	$19,015

See accompanying notes to condensed consolidated financial statements.

SPS TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited-Thousands of dollars, except share data)

1. Financial Statements

In the opinion of the Company's management, the accompanying unaudited, condensed consolidated financial statements contain all adjustments necessary to present fairly the financial position as of September 30, 2002, the results of operations for the three and nine month periods ended September 30, 2002 and 2001,

and cash flows for the nine month period ended September 30, 2002 and 2001. The December 31, 2001 balance sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America. The accompanying financial statements contain only normal recurring adjustments. All financial information has been prepared in conformity with the accounting principles reflected in the financial statements included in the 2001 Annual Report filed on Form 10-K applied on a consistent basis except as disclosed in Note 2.

2. Change in Accounting Policies

Effective January 1, 2002, the Company adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets." This statement requires that goodwill and intangible assets deemed to have an indefinite life no longer be amortized but be tested for impairment at least annually. The amortization period of intangible assets with finite lives is no longer limited to forty years. Total amortization expense for goodwill and intangible assets deemed to have an indefinite life for full year 2001 was $5,011 on an after-tax basis, or $0.38 per share. The Company incurred no transitional impairment charge for adopting the new provisions for determining goodwill impairment and assessing the useful lives of other intangible assets.

The following information is presented to compare current period net earnings to prior period net earnings adjusted to exclude amortization of goodwill and other intangible assets deemed to have an indefinite life that are no longer amortized beginning January 1, 2002:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2002	2001	2002	2001
Net earnings (loss):				
Reported net earnings (loss)	$(6,310)	$ 8,360	$ 2,370	$ 25,790
Goodwill amortization, net of tax	-	1,263	-	3,740
Adjusted net earnings (loss)	$(6,310)	$ 9,623	$ 2,370	$ 29,530
Basic earnings (loss) per share:				
Reported net earnings (loss)	$ (0.48)	$ 0.64	$ 0.18	$ 1.99

Goodwill amortization, net of tax	-	.09	-	.28
Adjusted net earnings (loss)	$ (0.48)	$ 0.73	$ 0.18	$ 2.27
Diluted earnings (loss) per share:				
Reported net earnings (loss)	$ (0.48)	$ 0.63	$ 0.18	$ 1.95
Goodwill amortization, net of tax	-	.09	-	.28
Adjusted net earnings (loss)	$ (0.48)	$ 0.72	$ 0.18	$ 2.23

Effective January 1, 2002, the Company also adopted the provisions of SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." This statement supersedes SFAS No. 121 on the same topic and the accounting and reporting provisions of APB Opinion No. 30, "Reporting the Results of Operations - Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions," for the disposal of a segment of a business. This statement also amends ARB No. 51, "Consolidated Financial Statements," to eliminate the exception to consolidate a subsidiary for which control is likely to be temporary. The adoption of this standard had no effect on the Company's financial statements.

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3. Restructure of Operations

In the third quarter of 2002, the Company announced plans to eliminate, consolidate and restructure certain manufacturing and distribution locations. The elements of this plan include headcount reductions, the closure of two manufacturing plants, the exit from certain distribution locations , cumulative translation adjustment write offs and further relocation of certain manufacturing activity to Asia. The Company's headcount will be reduced by approximately 300 employees in connection with these actions. The Statement of Consolidated Operations for the three months ended September 30, 2002 includes charges that total $16,000 ($11,200 or $0.85 per share on an after-tax basis) for restructurings and impairments, related inventory write downs and costs to mark two interest rate swaps, that recently became ineffective as a result of lower debt levels, to market. In addition, the Company has estimated that it will incur approximately $1,500 ($1,000 or $0.08 per share on an after-tax basis) for costs to wind down operations and transfer equipment related to these actions that will be charged to the Statement of Consolidated Operations as incurred. As of September 30, 2002, employment has been reduced by 46 people due to these actions.

In the second quarter of 2002, the Company announced plans to close a marketing and distribution center in Singapore and a tool manufacturing facility in France. The Statement of Consolidated Operations for the three months ended June 30, 2002 included charges for restructurings and impairments of $900 ($690 or $0.05 per share on an

after-tax basis). The Company's headcount was reduced by approximately 30 employees in connection with these actions.

In 2001, the Company announced plans to eliminate, consolidate and restructure certain manufacturing operations. The elements of this plan included the closure of five manufacturing plants (affecting 526 employees), reduction of an additional 270 employees at remaining plants, relocation of certain product lines to existing facilities, outsourcing the manufacture of certain product lines to third parties, discontinuing production of certain product lines and further integrating and consolidating the operations of certain acquired companies. The Statement of Consolidated Operations for the three months ended June 30, 2001 included charges for restructurings and impairments (including related inventory write downs of $1,500) that total $10,600 ($7,000 or $0.53 per share on an after-tax basis). The Statement of Consolidated Operations for the three months ended December 31, 2001 included charges for restructurings and impairments that total $10,000 ($6,500 or $0.49 per share on an after-tax basis). As of September 30, 2002 employment has been reduced by approximately 790 people due to these restructuring actions.

The following table summarizes the activity related to the Company's restructuring plans and the balances in the accrued restructure account:

	2002 Charges					
	Accrual December 31, 2001	2002 Plan	Adjust-ments to Prior Plan	Total	2002 Incurred	Accrual September 30, 2002
Restructurings and impairments:						
Employee separations	$ 3,335	$ 5,770	$(304)	$ 5,466	$ 3,410	$ 5,391
Cumulative translation adjustment write offs	-	7,516	-	7,516	7,516	-
Write downs of PP&E	-	582	425	1,007	1,007	-
Lease termination cost	600	-	(190)	(190)	310	100
Loss on sale of Lake Erie Design	-	-	309	309	309	-
Other costs	874	379	13	392	810	456
	4,809	14,247	253	14,500	13,362	5,947

Cost of goods sold:						
Write downs of inventory	-	1,091	409	1,500	1,500	-
Other Expense:						
Market value of ineffective interest rate swaps	-	900	-	900	900	-
	$ 4,809	$16,238	$ 662	$16,900	$15,762	$ 5,947

In addition, the Company has incurred certain restructure related costs that are charged to the Statement of Consolidated Operations as incurred. For the nine months ended September 30, 2002, the Company incurred $3,052 ($1,960 or $0.15 per share on an after-tax basis) of costs related to the restructure plan that were charged to the Statement of Consolidated Operations as incurred. These costs included $1,693 for losses during the wind-down period for facilities that were closed, $1,019 of costs to relocate equipment and $340 of costs to start up production at plants where products have been transferred. For the nine months ended September 30, 2001, the Company incurred $1,240 ($830 or $0.06 per share on an after-tax basis) of costs related to the restructure plan that were charged to the Statement of Consolidated Operations as incurred. These costs included $1,001 for losses during the wind-down period for plants that were closed and $239 for costs to relocate equipment.

4. Business Acquisitions

All acquisitions have been accounted for under the purchase method. The results of operations of the acquired businesses are included in the consolidated financial statements from the dates of acquisition.

On April 5, 2001, the Company acquired all of the outstanding stock of M. Argüeso & Co., Inc. (Argüeso) based in Mamaroneck, New York for $19,685. Consideration consisted of $9,094 in cash, $3,616 in debt assumed and 192,487 shares of the Company's common stock valued at $6,975. Argüeso is a manufacturer and distributor of wax blends for use in the investment casting industry. Argüeso's products are used in a variety of investment casting applications in industries such as aerospace, power generation and medical. The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition:

Current assets	$ 8,439
Property, plant and equipment	6,235
Intangible assets	750
Goodwill	7,843
Total assets acquired	23,267

Current liabilities	3,582
Net assets acquired	$19,685

Intangible assets acquired include patents valued at $750 with a 14 year weighted-average useful life. The goodwill of $7,843 was assigned to the Specialty Materials and Alloys segment and is not expected to be deductible for tax purposes.

In 2001, the Company also completed two relatively smaller acquisitions. On February 6, 2001, the Company and a group of investors acquired substantially all of the assets and business of AAA Aircraft Supply Co., Inc. (AAA) located in Windsor Locks, Connecticut for $7,000. At the time of acquisition, the Company's ownership percentage was 88.75 percent. In connection with the acquisition of AAA, members of AAA's management and a director of the Company obtained ownership interests in AAA of 6.25 percent and 5.0 percent, respectively, on the same terms as the Company. AAA is a North American distributor of fasteners sold to the aerospace markets. On October 3, 2001, the Company acquired substantially all the assets and business of J. F. McCaughin Co. (McCaughin) located in Rosemead, California for approximately $2,500. McCaughin is a formulator, manufacturer and distributor of waxes, supplies and equipment to the investment casting industry.

The following unaudited pro forma consolidated results of operations are presented as if the Argüeso acquisition had been made at the beginning of the periods presented. The effects of the AAA and McCaughin acquisitions are not material and, accordingly, have been excluded from the pro forma presentation.

	Nine Months Ended September 30,	
	2002	2001
Net sales	$628,783	$715,877
Net earnings	2,370	25,865
Basic earnings per common share	0.18	1.99
Diluted earnings per common share	0.18	1.96

The pro forma consolidated results of operations include adjustments to give effect to amortization of patents, interest expense on acquisition debt, shares of common stock issued and the related income tax effects. The unaudited pro forma information is not necessarily indicative of the results of operations that would have occurred had the purchase been made at the beginning of the periods presented or the future results of the combined operations.

5. Inventories

	September 30, 2002	December 31, 2001

Finished goods	$ 68,154	$ 75,667
Work-in-process	59,816	57,592
Raw materials and supplies	30,476	34,956
Tools	6,452	6,936
	$ 164,898	$ 175,151

6. Intangible Assets

	September 30, 2002	December 31, 2001
Gross carrying amount of amortized intangible assets:		
Patents	$2,483	$2,483
Customer Contracts	1,300	1,300
	$3,783	$3,783
Accumulated amortization of amortized intangible assets:		
Patents	$ 436	$ 286
Customer Contracts	442	155
	$ 878	$ 441

	Nine Months Ended September 30, 2002	Nine Months Ended September 30, 2001
Aggregate amortization expense	$ 437	$ 233

Estimated amortization expense:	Annual Amounts
For the year ended December 31, 2002	$585
For the year ended December 31, 2003	$585
For the year ended December 31, 2004	$585
For the year ended December 31, 2005	$203

For the year ended December 31, 2006 $203

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7. Goodwill

The changes in the carrying amount of goodwill for the nine months ended September 30, 2002, are as follows:

	Aerospace Fasteners and Components	Engineered Fasteners and Components	Specialty Materials and Alloys	Magnetic Products	Total
Balance as of January 1, 2002	$ 84,869	$ 77,364	$ 17,115	$ 27,224	$206,572
Foreign currency translation adjustments	2,388	190	-	-	2,578
Balance as of September 30, 2002	$ 87,257	$ 77,554	$ 17,115	$ 27,224	$209,150

8. Long-term Debt

On June 18, 2002, the Company entered into a Bank Credit Agreement to borrow up to $130,000 in either United States Dollars or certain European currencies. Borrowings bear interest at either a) an overnight base rate equal to the higher of the prime rate of the agent bank or the federal funds rate plus .5 percentage points, b) a rate equal to the effective interbank rate plus a margin ranging from 1.00 to 1.50 percentage points based on the consolidated Leverage Ratio, as defined, or c) at a rate and term negotiated between the agent bank and the Company, as applicable. Borrowings outstanding under the 2002 Bank Credit Agreement at September 30, 2002 were $30,000 with an interest rate of 2.885 percent. However, the Company utilizes interest rate swap agreements which effectively converted the variable rate borrowings under the 2002 Bank Credit Agreement to an average fixed rate of 7.775 percent. The 2002 Bank Credit Agreement expires June 30, 2005. The Company is required to pay a fee on unborrowed amounts of the facility ranging from .20 to .325 percentage points based on its consolidated Leverage Ratio. In connection with this Bank Credit Agreement, the 1998 Bank Credit Agreement and the 2000 Bank Credit Agreement were terminated.

The Company is subject to a number of restrictive covenants under its various debt agreements. Covenants associated with the Bank Credit Agreement are generally more restrictive than those of the Note Purchase Agreements. The following significant covenants are currently in place under the Bank Credit Agreement: maintenance of a consolidated debt-to-total capitalization (shareholders' equity plus total debt) ratio of not more than 50 percent, maintenance of a consolidated net worth of at least $282,148 plus 50 percent of consolidated net income for quarters ended after December 31, 2001 and maintenance of a Consolidated Fixed Charge Coverage Ratio, as defined, of not less than 1.25 to 1 (per the amended agreement dated September 26, 2002), except for the fiscal quarters ending September 30, 2002 and December 31, 2002 in respect of which such Consolidated fixed Charge

Coverage Ratio shall be not less than 1.10 to 1, for the prior four consecutive fiscal quarters as measured at the end of each quarter. Under the Note Purchase Agreements, restricted payments, which include all dividends and purchases or retirements of capital stock, made by the Company may not exceed $40,000 plus 50 percent of consolidated net income (or minus 100 percent of the consolidated net loss) from January 1, 1999 to the date of the restricted payment. As of September 30, 2002, the amount of retained earnings available for future restricted payments is $90,000. Certain of the Company's debt agreements contain cross default and cross acceleration provisions. At September 30, 2002, the Company was in compliance with all covenants. As of September 30, 2002, under the terms of the existing credit agreements, the Company is permitted to incur an additional $143,000 in debt.

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9. Commitments and Contingencies

Environmental Contingency

The Company has been identified as a potentially responsible party by various federal and state authorities for clean up or removal of waste from various disposal sites. At September 30, 2002, the accrued liability for environmental remediation represents management's best estimate of the undiscounted costs related to environmental remediation which are considered probable and can be reasonably estimated. The Company has not included any insurance recovery in the accrued environmental liability. The measurement of the liability is evaluated quarterly based on currently available information. Management believes the overall costs of environmental remediation will be incurred over an extended period of time. As the scope of the Company's environmental liability becomes more clearly defined, it is possible that additional reserves may be necessary. Accordingly, it is possible that the Company's results of operations in future quarterly or annual periods could be materially affected. Management does not anticipate that its consolidated financial condition will be materially affected by environmental remediation costs in excess of amounts accrued.

Litigation

The Company is involved in lawsuits, claims, investigations and proceedings, including commercial, environmental and employment matters, which arise in the ordinary course of business. Although the final outcome of these matters cannot be determined, it is management's opinion that the final resolution of these matters will not have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

On April 29, 2002, in the case of Brookover v. Flexmag Industries, Inc., an Ohio Appeals Court affirmed a trial court judgment against one of the Company's subsidiaries, resulting from a workplace injury claim in 1997. On June 17, 2002 the Company settled its portion of the claim for $2,150 ($1,328 after tax or $0.10 per share).

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10. Per Share Data

Basic earnings per common share is calculated using the average shares of common stock outstanding, while diluted earnings per common share reflects the potential dilution that could occur if stock options were exercised. Earnings per share are computed as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2002	2001	2002	2001
Net earnings (loss)	$ (6,310)	$ 8,360	$ 2,370	$ 25,790
Average shares of common stock outstanding used to compute basic earnings (loss)per common share	13,161,581	13,100,600	13,144,768	12,987,307
Additional common shares to be issued assuming exercise of stock options, net of shares assumed reacquired (a)	54,716	198,416	101,272	242,738
Shares used to compute dilutive effect of stock options	13,216,297	13,299,016	13,246,040	13,230,045
Basic earnings (loss) per common share	$ (0.48)	$ 0.64	$ 0.18	$ 1.99
Diluted earnings (loss) per common share	$ (0.48)	$ 0.63	$ 0.18	$ 1.95

(a) The computation of diluted loss per share for the three months ended September 30, 2002 excluded the potential common shares of 54,716 because these shares would have had an antidilutive effect on diluted loss per share.

Options to purchase 947,288 shares of common stock at a weighted-average price of $39.49 per share were outstanding during 2002 but were not included in the computation of diluted EPS for the three months ended

September 30, 2002 because the options' exercise price was greater than the average market price of the common shares. These options expire on various dates between February 10, 2007 and February 13, 2012.

Options to purchase 360,031 shares of common stock at a weighted-average price of $44.40 per share were outstanding during 2002 but were not included in the computation of diluted EPS for the nine months ended September 30, 2002 because the options' exercise price was greater than the average market price of the common shares. These options expire on various dates between December 17, 2007 and July 31, 2011.

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11. Segment Information

The Company has four reportable segments: Aerospace Fasteners and Components, Engineered Fasteners and Components, Specialty Materials and Alloys and Magnetic Products. The Aerospace Fasteners and Components segment consists of business units which produce precision fasteners and fastening systems and structural and other metal components for critical applications in the aerospace markets. The Engineered Fasteners and Components segment consists of business units which produce precision fasteners and fastening systems, structural and other metal components and consumable tools for critical applications in the automotive and industrial machinery markets. The Specialty Materials and Alloys segment produces specialty metals, superalloys and wax blends for aerospace, industrial gas turbine, medical and other general industrial applications. The Magnetic Products segment produces magnetic materials and products used in automotive, telecommunications, aerospace, reprographic, computer and advertising specialty applications.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2002	2001	2002	2001
Net sales:				
Aerospace Fasteners and Components	$ 76,123	$ 90,214	$230,823	$269,294
Engineered Fasteners and Components	73,966	68,413	221,001	216,641
Specialty Materials and Alloys	28,547	46,163	94,297	131,469
Magnetic Products	26,489	27,034	82,662	92,962
Total net sales	$205,125	$231,824	$628,783	$710,366

Operating earnings(loss):

Aerospace Fasteners and Components	$ 5,216	$ 10,413	$ 17,469	$ 29,640
Engineered Fasteners and Components	(7,598)	3,120	(1,744)	8,776
Specialty Materials and Alloys	3,393	5,820	11,928	18,849
Magnetic Products	(945)	743	397	4,511
Unallocated Corporate Costs	(3,350)	(2,670)	(9,640)	(8,720)
Total operating earnings (loss)	$ (3,284)	$ 17,426	$ 18,410	$ 53,056

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12. Recently Issued Accounting Standards

In June 2001, the Financial Accounting Standards Board issued SFAS No. 143, "Accounting for Asset Retirement Obligations." This statement requires that obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs be recognized when they are incurred and displayed as liabilities. This statement is effective for fiscal years beginning after June 15, 2002. The Company estimates that the impact of adopting this standard in the first quarter of 2003 will not be material.

In April 2002, SFAS No. 145, "Rescission of FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13, and Technical Corrections" was issued. This statement provides guidance on the classification of gains and losses from the extinguishment of debt and on the accounting for certain specified lease transactions. The adoption of this statement will not have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In June 2002, SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" was issued. This statement provides guidance on the recognition and measurement of liabilities associated with disposal activities and is effective for the Company on January 1, 2003.

SPS TECHNOLOGIES, INC. AND SUBSIDIARIES

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

Introduction

The Company's operating earnings decreased compared to the corresponding periods in the prior year. The reduction in earnings is primarily due to lower revenues in three of the Company's four segments compared to last year, particularly in those businesses that serve the aerospace, industrial gas turbine and electronics markets and nonrecurring restructure and impairment charges of $16.9 million. In September 2002, the Company announced plans to eliminate, consolidate and restructure certain of its operations. The Company expects to realize significant cost savings in connection with these actions, including a decrease in its employment cost structure of approximately $13.2 million. In 2002, the Company also continued to execute various steps of the restructuring plans announced in 2001.

Net Sales and Orders

Net sales decreased $26.7 million, or 11.5 percent in the third quarter of 2002 and $81.6 million, or 11.5 percent, for the nine months ended September 30, 2002 compared to the same periods in 2001. Incoming orders for the third quarter of 2002 were $200.4 million compared to $215.8 million for the third quarter of 2001, a 7.1 percent decrease. Incoming orders for the nine months ended September 30, 2002 were $620.9 million compared to $724.7 million for the same period in 2001, a 14.3 percent decrease.

Revenues of the Company's Aerospace Fasteners and Components segment decreased $14.1 million, or 15.6 percent, in the third quarter of 2002 and $38.5 million, or 14.3 percent, for the nine months ended September 30, 2002 compared to the same periods in 2001. Incoming orders for this segment decreased $21.0 million, or 23.4 percent, in the third quarter of 2002 and $85.0 million, or 28.5 percent, for the nine months ended September 30, 2002 compared to the same periods in 2001. The Company is experiencing the impacts of a cyclical downturn in the commercial aerospace industry. Weak demand for air travel, reduced airline flight schedules and poor financial results reported by the major North American airlines have influenced the reduced production schedules announced by commercial aircraft and jet engine manufacturers. The Company expects further weakening of demand for products produced by the Aerospace fastener and components segment for the balance of this year. Aerospace market conditions are not expected to improve during 2003.

Sales of recently acquired businesses (M. Argüeso & Co., Inc. on April 5, 2001 and J.F. McCaughin Co. on October 3, 2001) increased Specialty Materials and Alloys segment sales for the nine months of 2002 by $5.5 million compared to the first nine months of 2001. Sales of a business sold in 2001 (Lake Erie Design Co., Inc. on December 31, 2001) reduced segment sales for the third quarter by $2.5 million and for the nine month period by $7.7 million compared to the same periods in 2001. Excluding the sales of these recently acquired and sold businesses, sales for this segment decreased $14.7 million, or 38.3 percent, in the third quarter of 2002 and $34.9 million, or 30.8 percent, for the nine months ended September 30, 2002 compared to the same periods in 2001. Excluding the orders of these recently acquired and sold businesses, this segment's incoming orders decreased $3.5 million, or 12.5 percent, in the third quarter of 2002 and $28.3 million, or 26.3 percent, for the nine months ended September 30, 2002 compared to the same periods in 2001. These lower sales and incoming orders are primarily the result of lower build rates for aerospace and industrial gas turbine engines and lower raw material prices which benefit customers through lower prices. In 2001, the Company announced plans to expand production capacity at its Cannon-Muskegon subsidiary. The expansion project is substantially complete and the new furnace has been tested and qualified by certain

customers. Production runs are expected to start in the fourth quarter of 2002.

Sales of the Company's Engineered Fasteners and Components segment increased $5.6 million, or 8.1 percent, in the third quarter of 2002 and $4.4 million, or 2.0 percent, for the nine months ended September 30, 2002 compared to the same periods in 2001. This segment's incoming orders increased $9.1 million, or 13.6 percent, in the third quarter of 2002 and $9.2 million, or 4.2 percent, for the nine months ended September 30, 2002 compared to the same periods in 2001. Although the industrial markets served by this segment continued to be weak during the first nine months of 2002, revenues in the Company's automotive fastener business in North America have contributed to the increase in sales and orders for this segment noted above. In addition, sales of the Company's formed component business have increased over prior year results. While the Company is encouraged by order rates for its automotive fastener and components business, it remains cautious with respect to the outlook for demand for these products for the balance of the year and into 2003.

Revenues in the Magnetic Products segment decreased $0.5 million, or 2.0 percent, in the third quarter of 2002 and $10.3 million, or 11.1 percent, for the nine months ended September 30, 2002 compared to the same periods in 2001. The decreases in sales compared to 2001 result from lower demand from the automotive, general industrial and electronic markets. The Company is encouraged by the increase in incoming orders for products manufactured by the Company's recently established facility in China. This segment's incoming orders increased $1.4 million, or 5.5 percent, in the third quarter and $2.0 million, or 2.4 percent, for the nine months ended September 30, 2002 compared to the same periods in 2001.

Operating Earnings

Operating earnings decreased $20.7 million, or 118 percent, in the third quarter of 2002 and $34.6 million, or 65.3 percent, for the nine month period ended September 30, 2002. The Company adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" on January 1, 2002. Due to adopting the new statement, the Company is no longer required to amortize goodwill and intangible assets deemed to have an indefinite life. In 2002, the Company recorded a charge of $2.15 million as a result of the settlement of a legal judgment in the second quarter of 2002. Additional information on the related litigation is provided below in the section entitled "Litigation". In connection with the restructure plans announced in 2002 and 2001, the Company has incurred charges to eliminate, consolidate and restructure certain operations, wind down losses of plants closed and other restructure related costs in 2002 and 2001.

The following pro forma information excludes the amortization of goodwill and intangible assets deemed to have an indefinite life, the charge recorded in the second quarter of 2002 for the settlement of a legal judgement and the expenses related to the Company's restructuring actions. The pro forma operating earnings presentation is intended to supplement and clarify the operating earnings by segment presented in Note 11 to the financial statements, "Segment Information". Additional information on the expenses related to the Company's restructuring actions in total and by segment is provided below in the section entitled "Summary of the Restructure Actions".

(In thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2002	2001	2002	2001

Pro Forma operating earnings excluding amortization of goodwill, non-recurring charges and wind-down losses:				
Aerospace Fasteners and Components	$ 7,225	$11,546	$21,130	$35,661
Engineered Fasteners and Components	3,320	3,866	10,764	15,869
Specialty Materials and Alloys	3,702	5,982	12,237	19,856
Magnetic Products	1,161	934	4,921	6,801
Unallocated Corporate Costs	(3,150)	(2,670)	(9,440)	(8,720)
	12,258	19,658	39,612	69,467
Amortization of goodwill	-	(1,540)	-	(4,571)
Legal settlement	-	-	(2,150)	-
Restructurings and impairments	(15,100)	-	(16,000)	(10,600)
Other nonrecurring charges and wind-down losses	(442)	(692)	(3,052)	(1,240)
Reported operating earnings (loss)	$(3,284)	$17,426	$18,410	$53,056

Excluding the amortization of goodwill and other nonrecurring items noted above, operating earnings of the Company decreased from $19.7 million, or 8.5 percent of sales, for the third quarter of 2001 to $12.3 million, or 6.0 percent of sales for the third quarter of 2002. Operating earnings of the Company decreased from $69.5 million, or 9.8 percent of sales, for the nine months ended September 30, 2001 to $39.6 million, or 6.3 percent of sales for the nine months of 2002. For the nine month period, operating profit margins declined in all four of the Company's operating segments.

Pro forma operating earnings of the Aerospace Fasteners and Components segment decreased $4.3 million, or 37.4

percent, in the third quarter of 2002 and $14.5 million, or 40.7 percent for the nine months ended September 30, 2002. The decrease in operating earnings is due to lower revenue for this segment and operational difficulties at the Company's structural component manufacturing facilities in Europe. With the anticipated continued weakness in revenues, management will continue to focus on cost containment and productivity improvement opportunities to maintain reasonable operating profit margins at the Company's aerospace fastener manufacturing facilities. The structural component manufacturing operations have experienced operating losses of approximately $2.0 million in the first six months of 2002. The Company has consolidated the management responsibilities for manufacturing and marketing efforts in the structural component business with the aerospace fastener operations to enhance the operating performance of this business unit. The operating results of the structural component manufacturing operations improved in the third quarter in comparison to the first six months and the Company expects further improvements in profitability in 2003.

Pro forma operating earnings of the Specialty Materials and Alloys segment decreased $2.3 million, or 38.1 percent, in the third quarter of 2002 and $7.6 million, or 38.4 percent, for the nine months ended September 30, 2002. Operating earnings as a percent of sales for the nine month periods have declined from 15.1 percent of sales in 2001 to 13.0 percent of sales in 2002. The decrease in earnings and margins is due primarily to the decrease in sales discussed above and favorable margin realization in 2001 on raw materials.

Pro forma operating earnings of the Engineered Fasteners and Components segment decreased from $15.9 million, or 7.3 percent of sales, for the nine months ended September 30, 2001, to $10.8 million, or 4.9 percent of sales, for the nine months ended September 30, 2002. Despite higher sales, operating earnings and margins decreased in this segment. Profitability in 2002 was adversely affected by excess operating costs (such as premium freight and outside inspection expenses) incurred to fill stronger than expected automotive fastener demand, slower than planned implementation of certain cost reduction initiatives and start-up inefficiencies on production transferred to the Company's facility in Shannon, Ireland.

Pro forma operating earnings of the Magnetic Products segment decreased from $6.8 million, or 7.3 percent of sales, for the first nine months of 2001 to $4.9 million, or 6.0 percent of sales, for the first nine months of 2002. This segment has been subject to decreasing sales, intense price competition and declining margins. Part of the Company's strategy to reduce costs in this segment is to increase the level of manufacturing activity in Asia. One plant is currently in operation in Asia and a second plant is currently being commissioned. Start-up costs associated with this business transfer have negatively impacted margins in the first nine months of 2002.

Summary of the Restructure Actions

As discussed in note 3 to the financial statements, the Company announced plans in 2002 and 2001 to eliminate, consolidate and restructure certain of its operations. The following table summarizes the 2002 expenses related to the Company's restructuring plans and the balances in the accrued restructure account:

		2002 Charges				
	Accrual December 31, 2001	2002 Plan	Adjust-ments to Prior Plan	Total	2002 Incurred	Accrual September 30, 2002

Restructurings and impairments:						
Employee separations	$ 3,335	$ 5,770	$(304)	$ 5,466	$ 3,410	$ 5,391
Cumulative translation adjustment write offs	-	7,516	-	7,516	7,516	-
Write downs of PP&E	-	582	425	1,007	1,007	-
Lease termination cost	600					