MUELLER INDUSTRIES INC
Form 10-Q
July 28, 2016

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

FORM 10-Q

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

For the quarterly period ended July 2, 2016 Commission file number 1–6770

MUELLER INDUSTRIES, INC.
(Exact name of registrant as specified in its charter)

Delaware	25-0790410
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

8285 Tournament Drive, Suite 150

Memphis, Tennessee	38125
(Address of principal executive offices)	(Zip Code)

(901) 753-3200
(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

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

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company

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

The number of shares of the Registrant's common stock outstanding as of July 25, 2016, was 57,172,780.

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MUELLER INDUSTRIES, INC.

FORM 10-Q

For the Quarterly Period Ended July 2, 2016

As used in this report, the terms "Company," "Mueller," and "Registrant" mean Mueller Industries, Inc. and its consolidated subsidiaries taken as a whole, unless the context indicates otherwise.

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PART I. FINANCIAL INFORMATION
Item 1. Financial Statements

MUELLER INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

(In thousands, except per share data)	For the Quarter Ended July 2, 2016	For the Quarter Ended June 27, 2015	For the Six Months Ended July 2, 2016	For the Six Months Ended June 27, 2015
Net sales	$544,071	$555,593	$1,076,880	$1,092,835
Cost of goods sold	456,060	470,365	902,702	931,199
Depreciation and amortization	9,061	8,188	17,981	16,041
Selling, general, and administrative expense	34,514	33,420	70,294	66,251
Gain on sale of assets	—	(15,376)	—	(15,376)
Severance	—	3,442	—	3,442
Operating income	44,436	55,554	85,903	91,278
Interest expense	(1,692)	(2,219)	(3,540)	(4,295)
Other income, net	515	265	760	370
Income before income taxes	43,259	53,600	83,123	87,353
Income tax expense	(14,005)	(19,738)	(28,126)	(31,151)
(Loss) income from unconsolidated affiliates, net of tax	(995)	—	1,927	—
Consolidated net income	28,259	33,862	56,924	56,202
Net income attributable to noncontrolling interests	(462)	(211)	(497)	(573)
Net income attributable to Mueller Industries, Inc.	$27,797	$33,651	$56,427	$55,629
Weighted average shares for basic earnings per share	56,511	56,247	56,489	56,220
Effect of dilutive stock-based awards	418	743	456	737
Adjusted weighted average shares for diluted earnings per share	56,929	56,990	56,945	56,957
Basic earnings per share	$0.49	$0.60	$1.00	$0.99
Diluted earnings per share	$0.49	$0.59	$0.99	$0.98
Dividends per share	$0.100	$0.075	$0.175	$0.150

See accompanying notes to condensed consolidated financial statements.

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MUELLER INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

	For the Quarter Ended		For the Six Months Ended	
(In thousands)	July 2, 2016	June 27, 2015	July 2, 2016	June 27, 2015
Consolidated net income	$28,259	$33,862	$56,924	$56,202
Other comprehensive income (loss), net of tax:				
Foreign currency translation	(10,186)	7,056	(11,297)	(1,348)
Net change with respect to derivative instruments and hedging activities	700 (1)	(903) (2)	1,294 (3)	(1,101) (4)
Net actuarial (gain) loss on pension and postretirement obligations	1,530 (5)	(647) (6)	2,702 (7)	769 (8)
Attributable to unconsolidated affiliates	1,438 (9)	—	1,438 (9)	—
Other, net	9	34	23	7
Total other comprehensive (loss) income	(6,509)	5,540	(5,840)	(1,673)
Consolidated comprehensive income	21,750	39,402	51,084	54,529
Comprehensive loss attributable to noncontrolling interests	123	520	862	175
Comprehensive income attributable to Mueller Industries, Inc.	$21,873	$39,922	$51,946	$54,704

See accompanying notes to condensed consolidated financial statements.

(1) Net of tax of $(266)
(2) Net of tax of $166
(3) Net of tax of $(487)
(4) Net of tax of $440
(5) Net of tax of $(522)
(6) Net of tax of $216
(7) Net of tax of $(920)
(8) Net of tax of $(286)
(9) Net of tax of $(812)

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MUELLER INDUSTRIES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

(In thousands, except share data)	July 2, 2016	December 26, 2015
Assets		
Current assets:		
Cash and cash equivalents	$283,161	$274,844
Accounts receivable, less allowance for doubtful accounts of $565 in 2016 and $623 in 2015	305,332	251,571
Inventories	249,954	239,378
Other current assets	27,276	34,608
Total current assets	865,723	800,401
Property, plant, and equipment, net	297,939	280,224
Goodwill, net	128,339	120,252
Intangible assets, net	39,050	40,636
Investment in unconsolidated affiliates	70,077	65,900
Other assets	19,347	31,388
Total assets	$1,420,475	$1,338,801
Liabilities		
Current liabilities:		
Current portion of debt	$16,226	$11,760
Accounts payable	105,138	88,051
Accrued wages and other employee costs	31,199	35,636
Other current liabilities	65,387	73,982
Total current liabilities	217,950	209,429
Long-term debt, less current portion	213,646	204,250
Pension liabilities	15,435	17,449
Postretirement benefits other than pensions	17,268	17,427
Environmental reserves	20,830	20,943
Deferred income taxes	13,644	7,161
Other noncurrent liabilities	2,930	2,440
Total liabilities	501,703	479,099
Equity		
Mueller Industries, Inc. stockholders' equity:		
Preferred stock - $1.00 par value; shares authorized 5,000,000; none outstanding	—	—
Common stock - $.01 par value; shares authorized 100,000,000; issued 80,183,004; outstanding 57,167,406 in 2016 and 57,158,608 in 2015	802	802
Additional paid-in capital	274,928	271,158
Retained earnings	1,110,010	1,063,543
Accumulated other comprehensive loss	(59,472)	(54,990)

Treasury common stock, at cost	(453,613)	(453,228)
Total Mueller Industries, Inc. stockholders' equity	872,655	827,285
Noncontrolling interests	46,117	32,417
Total equity	918,772	859,702
Commitments and contingencies	—	—
Total liabilities and equity	$1,420,475	$1,338,801

See accompanying notes to condensed consolidated financial statements.

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MUELLER INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(In thousands)	For the Six Months Ended July 2, 2016	June 27, 2015
Cash flows from operating activities		
Consolidated net income	$56,924	$56,202
Reconciliation of consolidated net income to net cash provided by operating activities:		
Depreciation and amortization	18,162	16,293
Stock-based compensation expense	2,874	2,966
Equity in earnings of unconsolidated affiliates	(1,927)	—
Gain on disposal of assets	(555)	(15,392)
Impairment charges	—	570
Deferred income taxes	3,548	(1,445)
Income tax benefit from exercise of stock options	(186)	(146)
Changes in assets and liabilities, net of businesses acquired:		
Receivables	(52,334)	(24,304)
Inventories	1,176	(5,252)
Other assets	17,009	6,963
Current liabilities	(1,314)	(19,629)
Other liabilities	(1,440)	(415)
Other, net	(72)	739
Net cash provided by operating activities	41,865	17,150
Cash flows from investing activities		
Capital expenditures	(10,248)	(15,969)
Acquisition of businesses, net of cash acquired	(20,533)	(35,978)
Net withdrawals from restricted cash balances	1,508	3,486
Proceeds from the sale of assets	1,482	5,518
Net cash used in investing activities	(27,791)	(42,943)
Cash flows from financing activities		
Repayments of long-term debt	(500)	(500)
Dividends paid to stockholders of Mueller Industries, Inc.	(9,887)	(8,435)
Issuance (repayment) of debt by joint ventures, net	4,426	(17,750)
Issuance of debt	2,000	—
Net cash received to settle stock-based awards	326	125
Income tax benefit from exercise of stock options	186	146
Net cash used in financing activities	(3,449)	(26,414)
Effect of exchange rate changes on cash	(2,308)	(780)

Increase (decrease) in cash and cash equivalents	8,317	(52,987)
Cash and cash equivalents at the beginning of the period	274,844	352,134
Cash and cash equivalents at the end of the period	$283,161	$299,147

See accompanying notes to condensed consolidated financial statements.

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MUELLER INDUSTRIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

General

Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted. Results of operations for the interim periods presented are not necessarily indicative of results which may be expected for any other interim period or for the year as a whole. This Quarterly Report on Form 10-Q should be read in conjunction with the Company's Annual Report on Form 10-K, including the annual financial statements incorporated therein.

The accompanying unaudited interim financial statements include all normal recurring adjustments which are, in the opinion of management, necessary for a fair presentation of the results for the interim periods presented herein. The fiscal six months ended July 2, 2016 contained 27 weeks, while the fiscal six months ended June 27, 2015 contained 26 weeks.

Note 1 – Earnings per Common Share

Basic per share amounts have been computed based on the average number of common shares outstanding. Diluted per share amounts reflect the increase in average common shares outstanding that would result from the assumed exercise of outstanding stock options and vesting of restricted stock awards, computed using the treasury stock method. Approximately 418 thousand and 24 thousand stock options were excluded from the computation of diluted earnings per share for the quarters ended July 2, 2016 and June 27, 2015, respectively, because they were antidilutive.

Note 2 – Acquisitions and Dispositions

Acquisitions

On April 26, 2016, the Company entered into an agreement providing for the purchase of a 60.0 percent equity interest in Jungwoo Metal Ind. Co., LTD (Jungwoo-Mueller) for approximately $21.8 million in cash. Jungwoo-Mueller manufactures copper-based pipe joining products and is headquartered in Seoul, South Korea and serves markets worldwide. It complements the Company's existing copper fittings businesses in the Piping Systems segment and is reported in the Company's Condensed Consolidated Financial Statements one month in arrears.

This acquisition was accounted for using the acquisition method of accounting whereby the total purchase price was allocated to tangible and intangible assets acquired and liabilities assumed based on respective fair values.

The fair value of the assets acquired totaled $50.1 million, consisting primarily of property, plant, and equipment of $25.9 million, inventories of $15.8 million, accounts receivable of $5.6 million, other current assets of $1.5 million and cash of $1.3 million. The fair value of the liabilities assumed totaled $17.3 million, consisting primarily of long-term debt of $8.7 million, accounts payable of $7.3 million, pension liabilities of $0.8 million, and other current liabilities of $0.5 million. Of the remaining purchase price, $3.6 million was allocated to non-deductible goodwill. The noncontrolling interest in Jungwoo-Mueller is $14.6 million. The purchase price allocation is provisional as of July 2, 2016 and subject to change upon completion of the final valuation of the long-lived assets and noncontrolling interest during the measurement period.

During the second quarter of 2015, the Company recognized approximately $3.4 million of severance costs related to the reorganization of Yorkshire Copper Tube, acquired in 2014.

The valuations of businesses acquired during 2015 have been finalized. During the second quarter of 2016, a deferred tax liability of $4.1 million was recorded that resulted from a basis difference in the long-lived assets acquired from Great Lakes Copper Ltd. This resulted in an increase in goodwill. There were no changes to the purchase price allocations for Turbotec Products, Inc. or Sherwood Valve LLC from the amounts presented in the Company's 2015 Annual Report on Form 10-K.

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Dispositions

On June 1, 2015, the Company sold certain assets. Simultaneously, the Company entered into a lease agreement with the purchaser of the assets for their continued use for a period of approximately 22 months (Lease Period).

The total sales price was $20.2 million, of which $5.0 million was received on June 1, 2015; the Company will receive $5.0 million on December 30, 2016 and the remaining $10.2 million will be received at the end of the Lease Period. This transaction resulted in a pre-tax gain of $15.4 million in the second quarter of 2015, or 17 cents per diluted share after tax. This gain was recognized in the Plumbing & Refrigeration segment.

Note 3 –Segment Information

During the first quarter of 2016, the Company made changes to its management reporting structure as a result of a change in the way the Chief Executive Officer, who serves as the Chief Operating Decision Maker, manages and evaluates the business, makes key operating decisions, and allocates resources. Previously, the Company had two reportable segments: Plumbing & Refrigeration and OEM. During the first quarter, the Company realigned its operating segments into three reportable segments: Piping Systems, Industrial Metals, and Climate. Management has recast certain prior period amounts to conform the current period presentation. Each of the reportable segments is composed of certain operating segments that are aggregated primarily by the nature of products offered as follows:

Piping Systems

Piping Systems is composed of the following operating segments: Domestic Piping Systems Group, Canadian Operations, European Operations, Trading Group, Mueller-Xingrong (the Company's Chinese joint venture), and Jungwoo-Mueller (the Company's South Korean joint venture). The Domestic Piping Systems Group manufactures copper tube and fittings, plastic fittings, and line sets. These products are manufactured in the U.S. Outside the U.S., the Canadian Operations manufacture copper tube and line sets and sell the products primarily in the U.S. and Canada, and the European Operations manufacture copper tube, which is sold primarily in Europe. The Trading Group manufactures pipe nipples and imports and resells brass and plastic plumbing valves, malleable iron fittings, faucets, and plumbing specialty products in the U.S. and Mexico. Mueller-Xingrong manufactures engineered copper tube primarily for air-conditioning applications in China. Jungwoo-Mueller manufactures copper-based joining products that are sold worldwide. The Piping System segment's products are sold primarily to plumbing, refrigeration, and air-conditioning wholesalers, hardware wholesalers and co-ops, building product retailers, and air-conditioning original equipment manufacturers (OEMs).

Industrial Metals

Industrial Metals is composed of the following operating segments: Brass Rod & Copper Bar Products, Impacts & Micro Gauge, and Brass Value-Added Products. These businesses manufacture brass rod, impact extrusions, and forgings, as well as a wide variety of end products including plumbing brass, automotive components, valves, fittings, and gas assemblies. These products are manufactured in the U.S. and sold primarily to OEMs in the U.S., many of which are in the industrial, construction, heating, ventilation, and air-conditioning, plumbing, and refrigeration markets.

Climate

Climate is composed of the following operating segments: Refrigeration Products, Fabricated Tube Products, Westermeyer, and Turbotec. These domestic businesses manufacture and fabricate valves and assemblies primarily for the heating, ventilation, air-conditioning, and refrigeration markets in the U.S.

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Summarized segment information is as follows:

(In thousands)	For the Quarter Ended July 2, 2016 Piping Systems	Industrial Metals	Climate	Corporate and Eliminations	Total
Net sales	$388,662	$127,737	$31,359	$ (3,687)	$544,071
Cost of goods sold	333,356	104,874	22,448	(4,618)	456,060
Depreciation and amortization	5,787	2,120	618	536	9,061
Selling, general, and administrative expense	16,560	3,619	2,456	11,879	34,514
Operating income	32,959	17,124	5,837	(11,484)	44,436
Interest expense					(1,692)
Other income, net					515
Income before taxes					$43,259

(In thousands)	For the Quarter Ended June 27, 2015 Piping Systems	Industrial Metals	Climate	Corporate and Eliminations	Total
Net sales	$379,750	$145,228	$31,498	$ (883)	$555,593
Cost of goods sold	326,338	120,808	24,134	(915)	470,365
Depreciation and amortization	5,335	1,643	614	596	8,188
Selling, general, and administrative expense	16,776	2,302	2,500	11,842	33,420
Gain on sale of assets	(15,376)	—	—	—	(15,376)
Severance	3,442	—	—	—	3,442
Operating income	43,235	20,475	4,250	(12,406)	55,554
Interest expense					(2,219)
Other income, net					265
Income before taxes					$53,600

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Segment information (continued):

(In thousands)	Piping Systems	Industrial Metals	Climate	Corporate and Eliminations	Total
	For the Six Months Ended July 2, 2016				
Net sales	$757,552	$262,258	$62,065	$ (4,995)	$1,076,880
Cost of goods sold	647,148	214,103	46,153	(4,702)	902,702
Depreciation and amortization	11,436	4,255	1,217	1,073	17,981
Selling, general, and administrative expense	34,850	6,864	4,979	23,601	70,294
Operating income	64,118	37,036	9,716	(24,967)	85,903
Interest expense					(3,540)
Other income, net					760
Income before taxes					$83,123

(In thousands)	Piping Systems	Industrial Metals	Climate	Corporate and Eliminations	Total
	For the Six Months Ended June 27, 2015				
Net sales	$741,232	$296,264	$57,309	$ (1,970)	$1,092,835
Cost of goods sold	639,028	248,532	45,401	(1,762)	931,199
Depreciation and amortization	10,522	3,298	1,039	1,182	16,041
Selling, general, and administrative expense	34,122	5,000	4,354	22,775	66,251
Gain on sale of assets	(15,376)	—	—	—	(15,376)
Severance	3,442	—	—	—	3,442
Operating income	69,494	39,434	6,515	(24,165)	91,278
Interest expense					(4,295)
Other income, net					370
Income before taxes					$87,353

(In thousands)	July 2, 2016	December 26, 2015
Segment assets:		
Piping Systems	$863,138	$811,343
Industrial Metals	160,655	153,102
Climate	66,383	61,672
General Corporate	330,299	312,684
	$1,420,475	$1,338,801

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Note 4 – Inventories

(In thousands)	July 2, 2016	December 26, 2015
Raw materials and supplies	$64,206	$58,987
Work-in-process	36,604	25,161
Finished goods	154,593	161,410
Valuation reserves	(5,449)	(6,180)
Inventories	$249,954	$239,378

Note 5 – Derivative Instruments and Hedging Activities

The Company's earnings and cash flows are subject to fluctuations due to changes in commodity prices, foreign currency exchange rates, and interest rates. The Company uses derivative instruments such as commodity futures contracts, foreign currency forward contracts, and interest rate swaps to manage these exposures.

All derivatives are recognized in the Condensed Consolidated Balance Sheets at their fair value. On the date the derivative contract is entered into, it is either a) designated as (i) a hedge of a forecasted transaction or the variability of cash flow to be paid or received (cash flow hedge), or (ii) a hedge of the fair value of a recognized asset or liability (fair value hedge) or b) not designated in a hedge accounting relationship, even though the derivative contract was executed to mitigate an economic exposure, as the Company does not enter into derivative contracts for trading purposes (economic hedge). Changes in the fair value of a derivative instrument that is qualified, designated and highly effective as a cash flow hedge are recorded in accumulated other comprehensive income (AOCI), to the extent effective, until they are reclassified to earnings in the same period or periods during which the hedged transaction affects earnings. Changes in the fair value of a derivative instrument that is qualified, designated and highly effective as a fair value hedge, along with the gain or loss on the hedged recognized asset or liability that is attributable to the hedged risk, are recorded in current earnings. Changes in the fair value of undesignated derivative instruments and the ineffective portion of designated derivative instruments are reported in current earnings.

The Company documents all relationships between hedging instruments and hedged items, as well as the risk-management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives that are designated as fair value hedges to specific assets and liabilities in the Condensed Consolidated Balance Sheets and linking cash flow hedges to specific forecasted transactions or variability of cash flow.

The Company also assesses, both at the hedge's inception and on an ongoing basis, whether the designated derivatives that are used in hedging transactions are highly effective in offsetting changes in cash flow or fair values of hedged items. When a derivative is determined not to be highly effective as a hedge or the underlying hedged transaction is no longer probable of occurring, hedge accounting is discontinued prospectively, in accordance with the derecognition criteria for hedge accounting.

Commodity Futures Contracts

Copper and brass represent the largest component of the Company's variable costs of production. The cost of these materials is subject to global market fluctuations caused by factors beyond the Company's control. The Company occasionally enters into forward fixed-price arrangements with certain customers; the risk of these arrangements is generally managed with commodity futures contracts. These futures contracts have been designated as cash flow hedges.

At July 2, 2016, the Company held open futures contracts to purchase approximately $22.3 million of copper over the next 18 months related to fixed price sales orders. The fair value of those futures contracts was a $1.7 million net gain position, which was determined by obtaining quoted market prices (level 1 within the fair value hierarchy). In the next 12 months, the Company will reclassify into earnings realized gains or losses relating to cash flow hedges. At July 2, 2016, this amount was approximately $979 thousand of deferred net gains, net of tax.

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The Company may also enter into futures contracts to protect the value of inventory against market fluctuations. These futures contracts have been designated as fair value hedges. At July 2, 2016, the Company held open futures contracts to sell approximately $15.5 million of copper over the next six months related to copper inventory. The fair value of those futures contracts was a $498 thousand net loss position, which was determined by obtaining quoted market prices (level 1 within the fair value hierarchy).

Interest Rate Swap

On February 20, 2013, the Company entered into a two-year forward-starting interest rate swap agreement with an effective date of January 12, 2015, and an underlying notional amount of $200.0 million, pursuant to which the Company receives variable interest payments based on one-month LIBOR and pays fixed interest at a rate of 1.4 percent. Based on the Company's current variable premium pricing on its Term Loan Facility, the all-in fixed rate as of the effective date is 2.7 percent. The interest rate swap will mature on December 11, 2017, and is structured to offset the interest rate risk associated with the Company's floating-rate, LIBOR-based Term Loan Facility Agreement. The swap was designated and accounted for as a cash flow hedge from inception.

The fair value of the interest rate swap is estimated based on the present value of the difference between expected cash flows calculated at the contracted interest rate and the expected cash flows at the current market interest rate using observable benchmarks for LIBOR forward rates at the end of the period (level 2 within the fair value hierarchy). Interest payable and receivable under the swap agreement is accrued and recorded as an adjustment to interest expense. The fair value of the interest rate swap was a $2.4 million loss position at July 2, 2016, and there was $1.5 million of deferred losses, net of tax, included in AOCI that are expected to be reclassified into interest expense over the term of the hedged item.

The Company presents its derivative assets and liabilities in the Condensed Consolidated Balance Sheets on a net basis by counterparty. The following table summarizes the location and fair value of the derivative instruments and disaggregates our net derivative assets and liabilities into gross components on a contract-by-contract basis:

	Asset Derivatives			Liability Derivatives		
		Fair Value			Fair Value	
(In thousands)	Balance Sheet Location	July 2, 2016	December 26, 2015	Balance Sheet Location	July 2, 2016	December 26, 2015
Hedging instrument:						
Commodity contracts - gains	Other current assets	$ 1,761	$ 60	Other current liabilities	$ 24	$ 238
Commodity contracts - losses	Other current assets	(85)	—	Other current liabilities	(522)	(1,864)
Interest rate swap	Other assets	—	—	Other liabilities	(2,407)	(1,692)
Total derivatives [1]		$ 1,676	$ 60		$ (2,905)	$ (3,318)

[1] Does not include the impact of cash collateral received from or provided to counterparties.

The following tables summarize the effects of derivative instruments on our Condensed Consolidated Statements of Income:

		Three Months Ended		Six Months Ended	
(In thousands)	Location	July 2, 2016	June 27, 2015	July 2, 2016	June 27, 2015
Fair value hedges:					
(Loss) gain on commodity contracts (qualifying)	Cost of goods sold	$(332)	$1,256	$(383)	$1,468
Gain (loss) on hedged item - Inventory	Cost of goods sold	288	(1,403)	350	(1,650)
Undesignated derivatives:					
Gain on commodity contracts (nonqualifying)	Cost of goods sold	1,326	1,046	1,820	1,279

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The following tables summarize amounts recognized in and reclassified from AOCI during the period:

	Three Months Ended July 2, 2016		
(In thousands)	Gain (Loss) Recognized in AOCI (Effective Portion), Net of Tax	Classification Gains (Losses)	Loss (Gain) Reclassified from AOCI (Effective Portion), Net of Tax
Cash flow hedges:			
Commodity contracts	$2,464	Cost of goods sold	$ (1,359)
Interest rate swap	(115)	Interest expense	59
Other	(349)	Other	—
Total	$2,000	Total	$ (1,300)

	Three Months Ended June 27, 2015		
(In thousands)	Gain (Loss) Recognized in AOCI (Effective Portion), Net of Tax	Classification Gains (Losses)	Loss (Gain) Reclassified from AOCI (Effective Portion), Net of Tax
Cash flow hedges:			
Commodity contracts	$(1,159)	Cost of goods sold	$ (81)
Interest rate swap	267	Interest expense	63
Other	7		—
Total	$(885)		$ (18)

	Six Months Ended July 2, 2016		
(In thousands)	Gain (Loss) Recognized in AOCI	Classification Gains (Losses)	Loss (Gain) Reclassified from AOCI (Effective Portion), Net

	(Effective Portion), Net of Tax		of Tax
Cash flow hedges:			
Commodity contracts	$3,337	Cost of goods sold	$ (1,291)
Interest rate swap	(585)	Interest expense	128
Other	(295)	Other	—
Total	$2,457		$ (1,163)

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Derivative instrument information (continued):

(In thousands)	Six Months Ended June 27, 2015 Gain (Loss) Recognized in AOCI (Effective Portion), Net of Tax	Classification Gains (Losses)	Loss (Gain) Reclassified from AOCI (Effective Portion), Net of Tax
Cash flow hedges:			
Commodity contracts	$ (885)	Cost of goods sold	$ 490
Interest rate swap	(765)	Interest expense	131
Other	(72)	Other	—
Total	$ (1,722)		$ 621

The Company enters into futures and forward contracts that closely match the terms of the underlying transactions. As a result, the ineffective portion of the open hedge contracts through July 2, 2016 was not material to the Condensed Consolidated Statements of Income.

The Company primarily enters into International Swaps and Derivatives Association master netting agreements with major financial institutions that permit the net settlement of amounts owed under their respective derivative contracts. Under these master netting agreements, net settlement generally permits the Company or the counterparty to determine the net amount payable for contracts due on the same date and in the same currency for similar types of derivative transactions. The master netting agreements generally also provide for net settlement of all outstanding contracts with a counterparty in the case of an event of default or a termination event. The Company does not offset fair value amounts for derivative instruments and fair value amounts recognized for the right to reclaim cash collateral. At July 2, 2016 and December 26, 2015, the Company had recorded restricted cash in other current assets of $1.0 million and $2.6 million, respectively, as collateral related to open derivative contracts under the master netting arrangements.

Note 6 – Investment in Unconsolidated Affiliates

The Company owns a 50 percent interest in Tecumseh Products Holdings LLC (Joint Venture), an unconsolidated affiliate that acquired Tecumseh Products Company (Tecumseh) during the third quarter of 2015. The Company also owns 50 percent interest in a second unconsolidated affiliate that provided financing to Tecumseh in conjunction with the acquisition. These investments are accounted for using the equity method of accounting as the Company can exercise significant influence but does not own a majority equity interest or otherwise control the respective entities. Under the equity method of accounting, these investments are stated at initial cost and are adjusted for subsequent additional investments and the Company's proportionate share of earnings or losses and distributions.

The Company records its proportionate share of the investees' net income or loss one quarter in arrears as income (loss) from unconsolidated affiliates, net of tax, in the Condensed Consolidated Statements of Income.

The following tables present summarized financial information derived from the Company's equity method investees' combined consolidated financial statements, which are prepared in accordance with U.S. GAAP.

(In thousands)

	March 31, 2016	September 30, 2015
Current assets	$248,511	$251,389
Noncurrent assets	119,900	112,156
Current liabilities	158,000	178,784
Noncurrent liabilities	70,237	63,643

	March 31, 2016	
(In thousands)	For the Quarter Ended	For the Six Months Ended
Net sales	$138,900	$290,500
Gross profit	19,500	37,500
Net income	(1,990)	3,854

Included in the equity method investees' net income for the six months ended March 31, 2016 is a gain of $17.1 million that resulted from the allocation of the purchase price, which was finalized during the quarter ended December 31, 2015. That gain was offset by restructuring and impairment charges of $5.3 million and net losses of $8.0 million.

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Note 7 –Benefit Plans

The Company sponsors several qualified and nonqualified pension plans and other postretirement benefit plans for certain of its employees. The components of net periodic benefit cost are as follows:

(In thousands)	For the Quarter Ended July 2, 2016	For the Quarter Ended June 27, 2015	For the Six Months Ended July 2, 2016	For the Six Months Ended June 27, 2015
Pension benefits:				
Service cost	$165	$228	$360	$500
Interest cost	1,969	2,027	3,944	4,081
Expected return on plan assets	(2,466)	(2,655)	(4,932)	(5,309)
Amortization of net loss	746	656	1,520	1,370
Net periodic benefit cost	$414	$256	$892	$642
Other benefits:				
Service cost	$60	$84	$122	$180
Interest cost	149	190	305	386
Amortization of prior service (credit) cost	(224)	1	(448)	3
Amortization of net gain	(20)	(16)	(18)	(13)
Net periodic benefit (income) cost	$(35)	$259	$(39)	$556

Note 8 – Commitments and Contingencies

The Company is involved in certain litigation as a result of claims that arose in the ordinary course of business, which management believes will not have a material adverse effect on the Company's financial position, results of operations, or cash flows. It may also realize the benefit of certain legal claims and litigation in the future; these gain contingencies are not recognized in the Condensed Consolidated Financial Statements.

Guarantees

Guarantees, in the form of letters of credit, are issued by the Company generally to assure the payment of insurance deductibles and certain retiree health benefits. The terms of guarantees are generally one year but are renewable annually as required. These letters are primarily backed by the Company's revolving credit facility. The maximum payments that the Company could be required to make under its guarantees at July 2, 2016 were $7.0 million.

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Note 9 – Income Taxes

The Company's effective tax rate for the second quarter of 2016 was 32 percent compared with 37 percent for the same period last year. The items impacting the effective tax rate for the second quarter of 2016 were primarily attributable to reductions for the U.S. production activities deduction of $1.0 million, and the effect of foreign tax rates lower than statutory tax rates of $1.4 million. These items were partially offset by the provision for state income taxes, net of the federal benefit, of $0.8 million and miscellaneous items totaling $0.5 million.

For the second quarter of 2015, the difference between the effective tax rate and the amount computed using the U.S. federal statutory tax rate was primarily attributable to increases for state income taxes, net of the federal benefit, of $1.4 million and miscellaneous items totaling $0.6 million. These items were partially offset by reductions for the U.S. production activities deduction of $1.2 million.

The Company's effective tax rate for the first half of 2016 was 34 percent compared with 36 percent for the same period last year. The items impacting the effective tax rate for the first half of 2016 were primarily attributable to reductions for the U.S. production activities deduction of $1.9 million and the effect of foreign tax rates lower than statutory tax rates of $2.5 million. These items were partially offset by the provision for state income taxes, net of the federal benefit, of $1.7 million, and miscellaneous items totaling $1.7 million.

For the first half of 2015, the difference between the effective tax rate and what would be computed using the U.S. federal statutory tax rate was attributable to increases for state income taxes, net of the federal benefit, of $2.2 million and miscellaneous other items totaling $1.0 million. These items were partially offset by reductions for the U.S. production activities deduction of $2.2 million and the effect of foreign income taxes lower than statutory tax rates and other foreign adjustments of $0.4 million.

The Company files a consolidated U.S. federal income tax return and numerous consolidated and separate-company income tax returns in many state, local, and foreign jurisdictions. The statute of limitations is open for the Company's federal tax return and most state income tax returns for 2012 and all subsequent years and is open for certain state and foreign returns for earlier tax years due to ongoing audits and differing statute periods. The Internal Revenue Service is currently auditing the Company's 2013 federal tax return. While the Company believes that it is adequately reserved for possible future audit adjustments, the final resolution of these examinations cannot be determined with certainty and could result in final settlements that differ from current estimates.

Note 10 – Accumulated Other Comprehensive Income

AOCI includes certain foreign currency translation adjustments from those subsidiaries not using the U.S. dollar as their functional currency, net deferred gains and losses on certain derivative instruments accounted for as cash flow hedges, adjustments to pension and OPEB liabilities, unrealized gains and losses on marketable securities classified as available-for-sale, and other comprehensive income attributable to unconsolidated affiliates.

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The following table provides changes in AOCI by component, net of taxes and noncontrolling interests (amounts in parentheses indicate debits to AOCI):

(In thousands)	For the Six Months Ended July 2, 2016 Cumulative Translation Adjustment	Unrealized (Losses)/Gains on Derivatives	Minimum Pension/OPEB Liability Adjustment	Other	Total
Balance at December 26, 2015	$(24,773)	$ (2,009)	$ (28,429)	$221	$(54,990)
Other comprehensive income (loss) before reclassifications	(9,939)	2,457	1,910	1,461	(4,111)
Amounts reclassified from AOCI	—	(1,163)	792	—	(371)
Net current-period other comprehensive income	(9,939)	1,294	2,702	1,461	(4,482)
Balance at July 2, 2016	$(34,712)	$ (715)	$ (25,727)	$1,682	$(59,472)

(In thousands)	For the Six Months Ended June 27, 2015 Cumulative Translation Adjustment	Unrealized (Losses)/Gains on Derivatives	Minimum Pension/OPEB Liability Adjustment	Other	Total
Balance at December 27, 2014	$(7,076)	$ (953)	$ (35,164)	$270	$(42,923)
Other comprehensive income (loss) before reclassifications	(947)	(1,722)	(229)	7	(2,891)
Amounts reclassified from AOCI	—	621	998	—	1,619
Net current-period other comprehensive income	(947)	(1,101)	769	7	(1,272)
Balance at June 27, 2015	$(8,023)	$ (2,054)	$ (34,395)	$277	$(44,195)

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Reclassification adjustments out of AOCI were as follows:

(In thousands)	Amount reclassified from AOCI For the Three Months Ended July 2, 2016	June 27, 2015	Affected line item
Unrealized losses/(gains) on derivatives:			
Commodity contracts	$(2,108)	$(111)	Cost of goods sold
Interest rate swap	92	98	Interest expense
	716	(5)	Income tax expense
	(1,300)	(18)	Net of tax
	—	—	Noncontrolling interests
	$(1,300)	$(18)	Net of tax and noncontrolling interests
Amortization of net loss and prior service cost on employee benefit plans	$502	$641	Selling, general, and administrative expense
	(122)	(164)	Income tax expense
	380	477	Net of tax
	—	—	Noncontrolling interests
	$380	$477	Net of tax and noncontrolling interests

(In thousands)	Amount reclassified from AOCI For the Six Months Ended July 2, 2016	June 27, 2015	Affected line item
Unrealized losses/(gains) on derivatives:			
Commodity contracts	$(1,871)	$651	Cost of goods sold
Interest rate swap	200	204	Interest expense
	508	(234)	Income tax expense
	(1,163)	621	Net of tax
	—	—	Noncontrolling interests
	$(1,163)	$621	Net of tax and noncontrolling

			interests
Amortization of net loss and prior service cost on employee benefit plans	$1,054	$1,360	Selling, general, and administrative expense
	(262)	(362)	Income tax expense
	792	998	Net of tax
	—	—	Noncontrolling interests
	$792	$998	Net of tax and noncontrolling interests

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Note 11 – Noncontrolling Interests

(In thousands)	Noncontrolling Interests
Balance at December 26, 2015	$ 32,417
Purchase of Jungwoo-Mueller	14,562
Net income attributable to noncontrolling interests	497
Other comprehensive loss attributable to noncontrolling interests, net of tax:	
Foreign currency translation	(1,359)
Balance at July 2, 2016	$ 46,117

Note 12 – Recently Issued Accounting Standards

In March 2016, the Financial Accounting Standards Board (FASB) issued ASU (Accounting Standards Update) No. 2016-09, Compensation – Stock Compensation (Topic 718): Improvement to Employee Share-Based Payment Accounting (ASU 2016-09). The ASU requires all income tax effects of awards to be recognized in the income statement when the awards vest or are settled. It will also allow a company to make a policy election to account for forfeitures as they occur. The guidance is effective for public business entities in interim and fiscal periods beginning after December 15, 2016. Early adoption is permitted, but all of the guidance must be adopted in the same period. The Company is in the process of evaluating the impact of ASU 2016-09 on its Condensed Consolidated Financial Statements.

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842) (ASU 2016-02). ASU 2016-02 requires an entity to recognize a right-of-use asset and lease liability for all leases with terms of more than 12 months. Recognition, measurement and presentation of expenses will depend on classification as a financing or operating lease. The amendments also require certain quantitative and qualitative disclosures about leasing arrangements. The ASU will be effective for interim and fiscal periods beginning after December 15, 2018. Early adoption is permitted. The updated guidance requires a modified retrospective adoption. The Company is still evaluating the effects that the provision of ASU 2016-02 will have on its Condensed Consolidated Financial Statements.

In April 2015, the FASB issued ASU No. 2015-03, Interest – Imputation of Interest (Topic 835-30): Simplifying the Presentation of Debt Issue Costs (ASU 2015-03). The ASU simplifies the presentation of debt issuance costs by requiring debt issuance costs related to a recognized debt liability to be presented on the balance sheet as a direct deduction from the debt liability rather than as a separate asset. In circumstances in which there is not an associated debt liability amount recorded in the financial statements when the debt issuance costs are incurred, they will be reported on the balance sheet as an asset until the debt liability is recorded. The guidance is effective for public business entities in interim and fiscal periods beginning after December 15, 2015. Retrospective application is required. The Company adopted ASU 2015-03 effective December 27, 2015. The adoption of the ASU did not have a material impact on the Company's Condensed Consolidated Financial Statements.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606) (ASU 2014-09). The ASU will supersede virtually all existing revenue recognition guidance under U.S. GAAP and will be effective for annual reporting periods beginning after December 15, 2017. The fundamental principles of the new guidance are that companies should recognize revenue in a manner that reflects the timing of the transfer of services to customers and the amount of revenue recognized reflects the consideration that a company expects to receive for the goods and services provided. The new guidance establishes a five-step approach for the recognition of revenue. The

Company is in the process of evaluating the impact of ASU 2014-09 on its Condensed Consolidated Financial Statements.

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

General Overview

We are a leading manufacturer of copper, brass, aluminum, and plastic products. The range of these products is broad: copper tube and fittings; line sets; brass and copper alloy rod, bar, and shapes; aluminum and brass forgings; aluminum impact extrusions; plastic fittings and valves; refrigeration valves and fittings; fabricated tubular products; and steel nipples. We also resell imported brass and plastic plumbing valves, malleable iron fittings, faucets and plumbing specialty products. Mueller's operations are located throughout the United States and in Canada, Mexico, Great Britain, South Korea and China.

During the first quarter of 2016, the Company made changes to its management reporting structure as a result of a change in the way the Chief Executive Officer, who serves as the Chief Operating Decision Maker, manages and evaluates the business, makes key operating decisions, and allocates resources. Previously, the Company had two reportable segments: Plumbing & Refrigeration and OEM. During the first quarter, the Company realigned its operating segments into three reportable segments: Piping Systems, Industrial Metals, and Climate. Management has recast certain prior period amounts to conform to the current period presentation. Each of the reportable segments is composed of certain operating segments that are aggregated primarily by the nature of products offered as follows:

- Piping Systems: The Piping Systems segment is composed of Domestic Piping Systems Group, Canadian Operations, European Operations, Trading Group, Mueller-Xingrong (our Chinese joint venture), and Jungwoo-Mueller (our South Korean joint venture). The Domestic Piping Systems Group manufactures and sells copper tube, copper and plastic fittings, line sets, and valves in North America. The Canadian Operations manufacture copper tube and line sets in Canada and sells the products primarily in the U.S. and Canada. European Operations manufacture copper tube in the United Kingdom, which is sold throughout Europe. The Trading Group manufactures pipe nipples and sources products for import distribution in North America. Mueller-Xingrong manufactures engineered copper tube primarily for air-conditioning applications; these products are sold primarily to OEMs located in China. Jungwoo-Mueller manufactures copper-based joining products that are sold worldwide. The Piping Systems segment sells products to wholesalers in the plumbing and refrigeration markets, distributors to the manufactured housing and recreational vehicle industries, building material retailers, and air-conditioning OEMs.

- Industrial Metals: The Industrial Metals segment is composed of Brass Rod & Copper Bar Products, Impacts & Micro Gauge, and Brass-Value Added Products. The segment manufactures and sells brass and copper alloy rod, bar, and shapes; aluminum and brass forgings; aluminum impact extrusions; and gas valves and assemblies. The segment manufactures and sells its products primarily to domestic OEMs in the industrial, construction, heating, ventilation, and air-conditioning, plumbing, and refrigeration markets.

- Climate: The Climate segment is composed of Refrigeration Products, Fabricated Tube Products, Westermeyer, and Turbotec. The segment manufactures and sells refrigeration valves and fittings and fabricated tubular products. The segment sells its products primarily to the heating, ventilation, air-conditioning, and refrigeration markets in the U.S.

New housing starts and commercial construction are important determinants of the Company's sales to the heating, ventilation, and air-conditioning, refrigeration, and plumbing markets because the principal end use of a significant portion of our products is in the construction of single and multi-family housing and commercial buildings. Repairs and remodeling projects are also important drivers of underlying demand for these products.

Residential construction activity has shown improvement in recent years, but remains at levels below long-term historical averages. Continued improvement is expected, but may be tempered by continuing low labor participation rates, the pace of household formations, and tighter lending standards. Per the U.S. Census Bureau, the June 2016 seasonally adjusted annual rate of new housing starts was 1.2 million, which was consistent with the June 2015 rate. Mortgage rates remain at historically low levels, as the average 30-year fixed mortgage rate was 3.67 percent for the first six months of 2016 and 3.85 percent for the twelve months ended December 2015.

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The private non-residential construction sector, which includes offices, industrial, health care and retail projects, has shown improvement since 2014. Per the U.S. Census Bureau, the actual (not seasonally adjusted) value of private nonresidential construction put in place was $389.9 billion in 2015 compared to $359.7 billion in 2014. The seasonally adjusted annual value of private non-residential construction put in place was $407.4 billion in May 2016 compared to the December 2015 rate of $393.9 billion and the May 2015 rate of $392.0 billion. We expect that most of these conditions will continue to improve.

Profitability of certain of the Company's product lines depends upon the "spreads" between the cost of raw material and the selling prices of its products. The open market prices for copper cathode and scrap, for example, influence the selling price of copper tube, a principal product manufactured by the Company. We attempt to minimize the effects on profitability from fluctuations in material costs by passing through these costs to our customers. Our earnings and cash flow are dependent upon these spreads that fluctuate based upon market conditions.

Earnings and profitability are also impacted by unit volumes that are subject to market trends, such as substitute products, imports, technologies, and market share. In our core product lines, we intensively manage our pricing structure while attempting to maximize our profitability. From time-to-time, this practice results in lost sales opportunities and lower volume. For plumbing systems, plastics are the primary substitute product; these products represent an increasing share of consumption. U.S. consumption of copper tube is still predominantly supplied by U.S. manufacturers. For certain air-conditioning and refrigeration applications, aluminum based systems are the primary substitution threat. We cannot predict the acceptance or the rate of switching that may occur. In recent years, brass rod consumption in the U.S. has declined due to the outsourcing of many manufactured products to offshore regions.

Results of Operations

Consolidated Results

The following table compares summary operating results for 2016 and 2015:

(In thousands)	Three Months Ended July 2, 2016	Three Months Ended June 27, 2015	Percent Change 2016 vs. 2015	Six Months Ended July 2, 2016	Six Months Ended June 27, 2015	Percent Change 2016 vs. 2015
Net sales	$544,071	$555,593	(2.1)%	$1,076.880	$1,092,835	(1.5)%
Operating income	44,436	55,554	(20.0)	85,903	91,278	(5.9)
Net income	27,797	33,651	(17.4)	56,427	55,629	1.4

The following are components of changes in net sales compared to the prior year:

	Quarter-to-Date 2016 vs. 2015	Year-to-Date 2016 vs. 2015
Net selling price in core product lines	(12.8)%	(13.4)%
Unit sales volume in core product lines	(2.0)	(1.6)
Acquisitions	14.0	13.9
Other	(1.3)	(0.4)

(2.1)%	(1.5)%

The decrease in net sales during the second quarter of 2016 was primarily due to (i) lower net selling prices of $71.4 million in our core product lines, primarily copper tube and brass rod, (ii) lower unit sales volume of $11.4 million, primarily in the Industrial Metals segment and at Mueller-Xingrong, and (iii) a decrease in net sales of $6.7 million in our non-core product lines. These decreases were offset by (i) $63.8 million of sales recorded by Great Lakes Copper Ltd. (Great Lakes), acquired in July 2015, (ii) $10.8 million of sales recorded by Sherwood Valve LLC (Sherwood), acquired in June 2015, and (iii) $3.2 million of sales recorded by Jungwoo Metal Ind. Co., LTD (Jungwoo-Mueller), acquired in April 2016.

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The decrease in net sales during the first half of 2016 was primarily due to (i) lower net selling prices of $146.5 million in our core product lines, (ii) lower unit sales volume of $17.3 million, primarily in the Industrial Metals segment and at Mueller-Xingrong, and (iii) a decrease in net sales of $4.8 million in our non-core product lines. These decreases were offset by (i) $121.2 million of sales recorded by Great Lakes, (ii) $23.1 million of sales recorded by Sherwood, (iii) $4.5 million of incremental sales recorded by Turbotec Products, Inc. (Turbotec), acquired in March 2015, and (iv) $3.2 million of sales recorded by Jungwoo-Mueller.

Net selling prices generally fluctuate with changes in raw material costs. Changes in raw material costs are generally passed through to customers by adjustments to selling prices. The following graph shows the Comex average copper price per pound by quarter for the current and prior fiscal years:

The following tables compare cost of goods sold and operating expenses as dollar amounts and as a percent of net sales for 2016 and 2015:

	Three Months Ended		Six Months Ended	
(In thousands)	July 2, 2016	June 27, 2015	July 2, 2016	June 27, 2015
Cost of goods sold	$456,060	$470,365	$902,702	$931,199
Depreciation and amortization	9,061	8,188	17,981	16,041
Selling, general and administrative expense	34,514	33,420	70,294	66,251
Gain on sale of assets	—	(15,376)	—	(15,376)
Severance	—	3,442	—	3,442
Operating expenses	$499,635	$500,039	$990,977	$1,001,557

	Three Months Ended		Six Months Ended	
	July 2, 2016	June 27, 2015	July 2, 2016	June 27, 2015
Cost of goods sold	83.8 %	84.7 %	83.8 %	85.2 %
Depreciation and amortization	1.7	1.5	1.7	1.5
Selling, general and administrative expense	6.3	6.0	6.5	6.0
Gain on sale of assets	—	(2.8)	—	(1.4)
Severance	—	0.6	—	0.3
Operating expenses	91.8 %	90.0 %	92.0 %	91.6 %

Q2 2016 compared to Q2 2015

The decrease in cost of goods sold was primarily due to the decrease in the average cost of copper, our principal raw material, partially offset by the increase in volume related to businesses acquired. Depreciation and amortization increased in the second quarter of 2016 primarily as a result of depreciation and amortization of long-lived assets of businesses acquired.Selling, general, and administrative expenses increased slightly for the second quarter of 2016 primarily as a result of incremental expenses of $2.6 million associated with businesses acquired during 2015 and 2016. This was offset by a reduction in employee compensation expenses, including incentive compensation, of $0.4 million. In addition, there were $1.0 million of equipment relocation costs and fixed asset impairment charges related to the rationalization of Yorkshire Copper Tube (Yorkshire) recorded in the second quarter of 2015.

During the second quarter of 2015, our operating results were positively impacted by a net gain of $15.4 million recorded on the sale of certain assets. This was offset by $3.4 million of severance charges related to the rationalization of Yorkshire.

Interest expense decreased slightly in the second quarter of 2016 primarily as a result of decreased borrowing costs at Mueller-Xingrong. Other income, net, for the first quarter of 2016 was consistent with the first quarter of 2015.

Our effective tax rate for the second quarter of 2016 was 32 percent compared with 37 percent for the same period last year. The items impacting the effective tax rate for the second quarter of 2016 were primarily attributable to reductions for the U.S. production activities deduction of $1.0 million and the effect of foreign tax rates lower than statutory tax rates of $1.4 million. These items were partially offset by the provision for state income taxes, net of the federal benefit, of $0.8 million and miscellaneous items totaling $0.5 million.

For the second quarter of 2015, the difference between the effective tax rate and the amount computed using the U.S. federal statutory tax rate was primarily attributable to increases for state income taxes, net of the federal benefit, of $1.4 million and miscellaneous items totaling $0.6 million. These items were partially offset by reductions for the U.S. production activities deduction of $1.2 million.

We own a 50 percent interest in Tecumseh Products Holdings LLC, an unconsolidated affiliate that acquired Tecumseh Products Company (Tecumseh) during the third quarter of 2015. We also own a 50 percent interest in a second unconsolidated affiliate that provided financing to Tecumseh in conjunction with the acquisition. We account for these investments using the equity method of accounting. For the second quarter of 2016, we recognized a loss of $1.0 million on these investments.

2016 YTD compared to 2015 YTD

The decrease in cost of goods sold was primarily due to the decrease in the average cost of copper, partially offset by the increase in volume related to businesses acquired. Depreciation and amortization increased slightly in the first half of 2016 primarily as a result of depreciation and amortization of long-lived assets of businesses acquired.Selling, general, and administrative expenses increased for the first half of 2016 primarily as a result of incremental expenses of $6.2 million associated with businesses acquired during 2015 and 2016. In addition, there was $1.3 million of equipment relocation costs and fixed asset impairment charges related to the rationalization of Yorkshire recorded in the first half of 2015.

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During the first half of 2015, our operating results were positively impacted by a net gain of $15.4 million recorded on the sale of certain assets. This was offset by $3.4 million of severance charges related to the rationalization of Yorkshire.

Interest expense decreased in the first half of 2016 primarily as a result of decreased borrowing costs at Mueller-Xingrong. Other income, net, for the first half of 2016 was consistent with the second quarter of 2015.

Our effective tax rate for the first half of 2016 was 34 percent compared with 36 percent for the same period last year. The items impacting the effective tax rate for the first half of 2016 were primarily attributable to reductions for the U.S. production activities deduction of $1.9 million and the effect of foreign tax rates lower than statutory tax rates of $2.5 million. These items were partially offset by the provision for state income taxes, net of the federal benefit, of $1.7 million, and miscellaneous items totaling $1.7 million.

For the first half of 2015, the difference between the effective tax rate and the amount computed using the U.S. federal statutory tax rate was attributable to increases for state income taxes, net of the federal benefit, of $2.2 million and miscellaneous other items totaling $1.0 million. These items were partially offset by reductions for the U.S. production activities deduction of $2.2 million and the effect of foreign income taxes lower than statutory tax rates and other foreign adjustments of $0.4 million.

During the first half of 2016, we recognized $1.9 million of income on our investment in unconsolidated affiliates. This included the gain that resulted from the allocation of the purchase price recorded by our equity method investees, which was offset by restructuring and impairment charges and operating losses.

Piping Systems Segment

The following table compares summary operating results for 2016 and 2015 for the businesses comprising our Piping Systems segment:

(In thousands)	Three Months Ended July 2, 2016	Three Months Ended June 27, 2015	Percent Change 2016 vs. 2015	Six Months Ended July 2, 2016	Six Months Ended June 27, 2015	Percent Change 2016 vs. 2015
Net sales	$388,662	$379,750	2.3 %	$757,552	$741,232	2.2 %
Operating income	32,959	43,235	(23.8)	64,118	69,494	(7.7)

The following are components of changes in net sales compared to the prior year:

	Quarter-to-Date 2016 vs. 2015	Year-to-Date 2016 vs. 2015
Net selling price in core product lines	(13.4)%	(14.0)%
Unit sales volume in core product lines	(0.7)	0.1
Acquisitions	17.7	16.8
Other	(1.3)	(0.7)

2.3	%	2.2 %

The increase in net sales during the second quarter of 2016 was primarily attributable to (i) $63.8 million of sales recorded by Great Lakes and (ii) $3.2 million of sales recorded by Jungwoo-Mueller. These increases were offset by (i) lower net selling prices of $51.0 million in the segment's core product lines, primarily copper tube, (ii) a decrease in net sales of $5.1 million in the segment's non-core product lines, and (iii) lower unit sales volume of $2.5 million in the segment's core product lines, primarily Mueller-Xingrong.

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The increase in net sales during the first half of 2016 was primarily due to (i) $121.2 million of sales recorded by Great Lakes and (ii) $3.2 million of sales recorded by Jungwoo-Mueller. These increases were offset by (i) lower net selling prices of $104.0 million in the segment's core product lines and (ii) a decrease in net sales of $4.8 million in the segment's non-core product lines.

The following tables compare cost of goods sold and operating expenses as dollar amounts and as a percent of net sales for 2016 and 2015:

	Three Months Ended		Six Months Ended	
(In thousands)	July 2, 2016	June 27, 2015	July 2, 2016	June 27, 2015
Cost of goods sold	$333,356	$326,338	$647,148	$639,028
Depreciation and amortization	5,787	5,335	11,436	10,522
Selling, general and administrative expense	16,560	16,776	34,850	34,122
Gain on sale of assets	—	(15,376)	—	(15,376)
Severance	—	3,442	—	3,442
Operating expenses	$355,703	$336,515	$693,434	$671,738

	Three Months Ended		Six Months Ended	
	July 2, 2016	June 27, 2015	July 2, 2016	June 27, 2015
Cost of goods sold	85.8%	85.9 %	85.4%	86.2 %
Depreciation and amortization	1.5	1.4	1.5	1.4
Selling, general and administrative expense	4.2	4.4	4.6	4.6
Gain on sale of assets	—	(4.0)	—	(2.1)
Severance	—	0.9	—	0.5
Operating expenses	91.5%	88.6 %	91.5%	90.6 %

The increase in cost of goods sold during the second quarter of 2016 was primarily due to the increase in volume related to Great Lakes and Jungwoo-Mueller, partially offset by the decrease in the average cost of copper. Depreciation and amortization increased slightly as a result of depreciation and amortization of the long-lived assets acquired at Great Lakes.Selling, general, and administrative expenses increased slightly for the second quarter of 2016, primarily as a result of incremental expenses associated with Great Lakes and Jungwoo-Mueller of $2.3 million. This was offset by a reduction in (i) sales commissions of $0.7 million, (ii) environmental remediation costs of $0.4 million, and (iii) employee compensation expenses, including incentive compensation, of $0.5 million. Lastly, there was $1.0 million of equipment relocation costs and fixed asset impairment charges related to the rationalization of Yorkshire recorded in the second quarter of 2015.

During the second quarter of 2015, the segment's operating results were positively impacted by a net gain of $15.4 million recorded on the sale of certain assets. This was offset by $3.4 million of severance charges related to the rationalization of Yorkshire.

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The increase in cost of goods sold during the first half of 2016 was primarily due to the increase in volume related to Great Lakes and Jungwoo-Mueller, partially offset by the decrease in the average cost of copper. Depreciation and amortization increased as a result of depreciation and amortization of the long-lived assets acquired at Great Lakes.Selling, general, and administrative expenses increased slightly for the first half of 2016, primarily due to incremental expenses associated with Great Lakes and Jungwoo-Mueller of $4.0 million. This was offset by a reduction in (i) sales commissions of $1.4 million and (ii) environmental remediation costs of $0.4 million. Lastly, there was $1.3 million of equipment relocation costs and fixed asset impairment charges related to the rationalization of Yorkshire recorded in the first half of 2015.

During the first half of 2015, the segment's operating results were positively impacted by a net gain of $15.4 million recorded on the sale of certain assets. This was offset by $3.4 million of severance charges related to the rationalization of Yorkshire.

Industrial Metals Segment

The following table compares summary operating results for 2016 and 2015 for the businesses comprising our Industrial Metals segment:

(In thousands)	Three Months Ended July 2, 2016	Three Months Ended June 27, 2015	Percent Change 2016 vs. 2015	Six Months Ended July 2, 2016	Six Months Ended June 27, 2015	Percent Change 2016 vs. 2015
Net sales	$127,737	$145,228	(12.0)%	$262,258	$296,264	(11.5)%
Operating income	17,124	20,475	(16.4)	37,036	39,434	(6.1)

The following are components of changes in net sales compared to the prior year:

	Quarter-to-Date 2016 vs. 2015	Year-to-Date 2016 vs. 2015
Net selling price in core product lines	(14.2)%	(14.3)%
Unit sales volume in core product lines	(6.1)	(6.1)
Acquisitions	7.5	7.8
Other	0.8	1.1
	(12.0)%	(11.5)%

The decrease in net sales during the second quarter of 2016 was primarily due to (i) lower net selling prices of $20.4 million in the segment's core product lines, primarily brass rod, and (ii) lower unit sales volume of $8.8 million in the segment's core product lines. These decreases were offset by $10.8 million of sales recorded by Sherwood.

The decrease in net sales during the first half of 2016 was primarily due to (i) lower unit sales volume of $42.5 million in the segment's core product lines, and (ii) lower net selling prices of $18.0 million in the segment's core product lines. These decreases were offset by $23.1 million of sales recorded by Sherwood.

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The following tables compare cost of goods sold and operating expenses as dollar amounts and as a percent of net sales for 2016 and 2015:

	Three Months Ended		Six Months Ended	
(In thousands)	July 2, 2016	June 27, 2015	July 2, 2016	June 27, 2015
Cost of goods sold	$104,874	$120,808	$214,103	$248,532
Depreciation and amortization	2,120	1,643	4,255	3,298
Selling, general and administrative expense	3,619	2,302	6,864	5,000
Operating expenses	$110,613	$124,753	$225,222	$256,830

	Three Months Ended		Six Months Ended	
	July 2, 2016	June 27, 2015	July 2, 2016	June 27, 2015
Cost of goods sold	82.1%	83.2 %	81.6%	83.9 %
Depreciation and amortization	1.7	1.1	1.6	1.1
Selling, general and administrative expense	2.8	1.6	2.7	1.7
Operating expenses	86.6%	85.9 %	85.9%	86.7 %

The decrease in cost of goods sold during the second quarter of 2016 was primarily due to the decrease in the average cost of copper. Depreciation and amortization increased slightly as a result of the long-lived assets acquired at Sherwood and recent capital expenditures. Selling, general, and administrative expenses increased primarily due to incremental expenses associated with Sherwood of $1.5 million.

The decrease in cost of goods sold during the first half of 2016 was primarily due to the decrease in the average cost of copper. Depreciation and amortization increased as a result of the long-lived assets acquired at Sherwood and recent capital expenditures.Selling, general, and administrative expenses increased primarily due to incremental expenses associated with Sherwood of $2.1 million, offset by a decrease in net periodic pension costs of $0.3 million.

Climate Segment

The following table compares summary operating results for 2016 and 2015 for the businesses comprising our Climate segment:

Three Months Ended