

MRC GLOBAL INC.
Form 10-Q
August 02, 2018

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2018

OR

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

FOR THE TRANSITION PERIOD FROM _____ TO _____

Commission file number: 001-35479

MRC Global Inc.
(Exact name of registrant as specified in its charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

20-5956993
(I.R.S. Employer
Identification No.)

Fulbright Tower

1301 McKinney Street, Suite 2300

Houston, Texas 77010
(Address of Principal Executive Offices) (Zip Code)

(877) 294-7574
(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 [] 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 [] No []

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

Large accelerated filer [] Accelerated filer [] Non-accelerated filer (do not check if a smaller reporting company) []

Smaller reporting company [] Emerging growth company []

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

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

The Company's common stock is traded on the New York Stock Exchange under the symbol "MRC". There were 90,315,224 shares of the registrant's common stock (excluding 87,247 unvested restricted shares), par value \$0.01 per share, issued and outstanding as of July 27, 2018.

Table Of Contents

INDEX TO QUARTERLY REPORT ON FORM 10-Q

| | |
|---|----|
| Page | |
| PART I – FINANCIAL INFORMATION | |
| ITEM 1. <u>financial statements (UNAUDITED)</u> | 1 |
| <u>Condensed Consolidated Balance Sheets – JUNE 30, 2018 and December 31, 2017</u> | 1 |
| <u>cONdENSED cONSOLIDATED STATEMENTS OF OPERATIONS – THREE AND SIX MONTHS ENDED JUNE 30, 2018 AND JUNE 30, 2017</u> | 2 |
| <u>Condensed Consolidated Statements of other cOMPREHENSIVE INCOME – three and six months ended JUNE 30, 2018 and JUNE 30, 2017</u> | 3 |
| <u>Condensed CONSOLIDATED STATEMENTS OF cash flows –Six MONTHS ENDED JUNE 30, 2018 and JUNE 30, 2017</u> | 4 |
| <u>Notes to the Condensed Consolidated Financial Statements – JUNE 30, 2018</u> | 5 |
| ITEM 2. <u>management’s discussion and analysis of financial condition and results of operations</u> | 14 |
| ITEM 3. <u>quantitative and qualitative disclosures about market risk</u> | 26 |
| ITEM 4. <u>controls and procedures</u> | 27 |
| PART II – OTHER INFORMATION | |
| ITEM 1. <u>LEGAL PROCEEDINGS</u> | 28 |
| ITEM <u>RISK FACTORS</u> | 28 |
| 1a. | |
| ITEM 2. <u>UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS</u> | 28 |
| ITEM 3. <u>Defaults Upon Senior Securities</u> | 28 |
| ITEM 4. <u>MINING SAFETY DISCLOSURES</u> | 29 |
| ITEM 5. <u>other information</u> | 29 |
| ITEM 6. <u>Exhibits</u> | 30 |

Table Of Contents

CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

MRC GLOBAL INC.

(in millions, except shares)

| | June 30, 2018 | December 31, 2017 |
|--|------------------|-------------------------|
| Assets | | |
| Current assets: | | |
| Cash | \$ 31 | \$ 48 |
| Accounts receivable, net | 676 | 522 |
| Inventories, net | 872 | 701 |
| Other current assets | 39 | 47 |
| Total current assets | 1,618 | 1,318 |
| Other assets | 21 | 21 |
| Property, plant and equipment, net | 147 | 147 |
| Intangible assets: | | |
| Goodwill, net | 485 | 486 |
| Other intangible assets, net | 345 | 368 |
| | \$ 2,616 | \$ 2,340 |
| Liabilities and stockholders' equity | | |
| Current liabilities: | | |
| Trade accounts payable | \$ 527 | \$ 415 |
| Accrued expenses and other current liabilities | 136 | 143 |
| Current portion of long-term debt | 4 | 4 |
| Total current liabilities | 667 | 562 |
| Long-term obligations: | | |
| Long-term debt, net | 704 | 522 |
| Deferred income taxes | 102 | 106 |
| Other liabilities | 38 | 36 |
| Commitments and contingencies | | |

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| | | |
|---|----------|----------|
| 6.5% Series A Convertible Perpetual Preferred Stock, \$0.01 par value; authorized 363,000 shares; 363,000 shares issued and outstanding | 355 | 355 |
| Stockholders' equity: | | |
| Common stock, \$0.01 par value per share: 500 million shares authorized, 104,923,720 and 103,099,692 issued, respectively | 1 | 1 |
| Additional paid-in capital | 1,714 | 1,691 |
| Retained deficit | (520) | (548) |
| Less: Treasury stock at cost: 14,622,930 and 11,751,726 shares, respectively | (225) | (175) |
| Accumulated other comprehensive loss | (220) | (210) |
| | 750 | 759 |
| | \$ 2,616 | \$ 2,340 |

See notes to condensed consolidated financial statements.

Table Of Contents

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

MRC GLOBAL INC.

(in millions, except per share amounts)

| | Three Months Ended | | Six Months Ended | |
|--|-----------------------|---------------------|------------------|------------------|
| | June 30, 2018 | June 30, 2017 | June 30, 2018 | June 30, 2017 |
| Sales | \$ 1,082 | \$ 922 | \$ 2,092 | \$ 1,784 |
| Cost of sales | 905 | 773 | 1,746 | 1,495 |
| Gross profit | 177 | 149 | 346 | 289 |
| Selling, general and administrative expenses | 136 | 132 | 274 | 258 |
| Operating income | 41 | 17 | 72 | 31 |
| Other expense: | | | | |
| Interest expense | (10) | (8) | (18) | (15) |
| Write off of debt issuance costs | (1) | - | (1) | - |
| Other, net | - | - | 2 | - |
| Income before income taxes | 30 | 9 | 55 | 16 |
| Income tax expense | 8 | 3 | 15 | 4 |
| Net income | 22 | 6 | 40 | 12 |
| Series A preferred stock dividends | 6 | 6 | 12 | 12 |
| Net income attributable to common stockholders | \$ 16 | \$ - | \$ 28 | \$ - |
| Basic income per common share | \$ 0.18 | \$ - | \$ 0.31 | \$ - |
| Diluted income per common share | \$ 0.17 | \$ - | \$ 0.30 | \$ - |
| Weighted-average common shares, basic | 90.1 | 94.5 | 90.7 | 94.6 |
| Weighted-average common shares, diluted | 91.6 | 95.6 | 92.7 | 96.0 |

See notes to condensed consolidated financial statements.

Table Of Contents

CONDENSED CONSOLIDATED STATEMENTS OF OTHER COMPREHENSIVE INCOME (UNAUDITED)

MRC GLOBAL INC.

(in millions)

| | Three Months Ended | | Six Months Ended | |
|---|--------------------------|---------------------|---------------------|---------------------|
| | June 30, 2018 | June 30, 2017 | June 30, 2018 | June 30, 2017 |
| Net income | \$ 22 | \$ 6 | \$ 40 | \$ 12 |
| Other comprehensive (loss) income | | | | |
| Foreign currency translation adjustments | (9) | 8 | (10) | 14 |
| Hedge accounting adjustments | 1 | - | - | - |
| Total other comprehensive (loss) income, net of tax | (8) | 8 | (10) | 14 |
| Comprehensive income | \$ 14 | \$ 14 | \$ 30 | \$ 26 |

See notes to condensed consolidated financial statements.

3

Table Of Contents

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

MRC GLOBAL INC.

(in millions)

| | Six Months Ended | |
|---|---------------------|---------------------|
| | June 30, 2018 | June 30, 2017 |
| Operating activities | | |
| Net income | \$ 40 | \$ 12 |
| Adjustments to reconcile net income to net cash used in operations: | | |
| Depreciation and amortization | 12 | 11 |
| Amortization of intangibles | 22 | 22 |
| Equity-based compensation expense | 7 | 9 |
| Deferred income tax benefit | (4) | (7) |
| Amortization of debt issuance costs | 1 | 2 |
| Write off of debt issuance costs | 1 | - |
| Increase in LIFO reserve | 22 | 6 |
| Foreign currency losses (gains) | 1 | (2) |
| Other | (1) | 4 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (157) | (117) |
| Inventories | (201) | (33) |
| Other current assets | 12 | 7 |
| Accounts payable | 116 | 68 |
| Accrued expenses and other current liabilities | (10) | (6) |
| Net cash used in operations | (139) | (24) |
| Investing activities | | |
| Purchases of property, plant and equipment | (9) | (14) |
| Net cash used in investing activities | (9) | (14) |
| Financing activities | | |
| Payments on revolving credit facilities | (475) | (223) |
| Proceeds from revolving credit facilities | 659 | 223 |
| Payments on long-term obligations | (2) | (4) |

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| | | |
|---|-------|-------|
| Debt issuance costs paid | (1) | - |
| Purchase of common stock | (50) | (18) |
| Dividends paid on preferred stock | (12) | (12) |
| Repurchases of shares to satisfy tax withholdings | (5) | (3) |
| Proceeds from exercise of stock options | 20 | - |
| Net cash provided by (used in) financing activities | 134 | (37) |
| Decrease in cash | (14) | (75) |
| Effect of foreign exchange rate on cash | (3) | 3 |
| Cash -- beginning of period | 48 | 109 |
| Cash -- end of period | \$ 31 | \$ 37 |
| Supplemental disclosures of cash flow information: | | |
| Cash paid for interest | \$ 18 | \$ 13 |
| Cash paid for income taxes | \$ 22 | \$ 22 |
| See notes to condensed consolidated financial statements. | | |

Table Of Contents

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MRC GLOBAL INC

NOTE 1 – BACKGROUND AND BASIS OF PRESENTATION

Business Operations: MRC Global Inc. is a holding company headquartered in Houston, Texas. Our wholly owned subsidiaries are global distributors of pipe, valves, fittings (“PVF”) and related products and services across each of the upstream (exploration, production and extraction of underground oil and gas), midstream (gathering and transmission of oil and gas, gas utilities, and the storage and distribution of oil and gas) and downstream (crude oil refining and petrochemical and chemical processing and general industrials) sectors. We have branches in principal industrial, hydrocarbon producing and refining areas throughout the United States, Canada, Europe, Asia, Australasia, the Middle East and Caspian. Our products are obtained from a broad range of suppliers.

Basis of Presentation: We have prepared our unaudited condensed consolidated financial statements in accordance with Rule 10-01 of Regulation S-X for interim financial statements. These statements do not include all information and footnotes that generally accepted accounting principles require for complete annual financial statements. However, the information in these statements reflects all normal recurring adjustments which are, in our opinion, necessary for a fair presentation of the results for the interim periods. The results of operations for the three and six months ended June 30, 2018 are not necessarily indicative of the results that will be realized for the fiscal year ending December 31, 2018. We have derived our condensed consolidated balance sheet as of December 31, 2017 from the audited consolidated financial statements for the year ended December 31, 2017. You should read these condensed consolidated financial statements in conjunction with the audited consolidated financial statements and notes thereto for the year ended December 31, 2017.

The consolidated financial statements include the accounts of MRC Global Inc. and its wholly owned and majority owned subsidiaries (collectively referred to as the “Company” or by such terms as “we,” “our” or “us”). All material intercompany balances and transactions have been eliminated in consolidation.

Recent Accounting Pronouncements: In February 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2016-02, Leases, which will replace the existing guidance in ASC 870, Leases. This ASU requires a dual approach for lessee accounting under which a lessee would account for leases as finance leases or operating leases. Both finance leases and operating leases will result in the lessee recognizing a right-of-use asset and a corresponding lease liability. For finance leases, the lessee would recognize interest expense and amortization of the right-of-use asset, and for operating leases, the lessee would recognize a straight-line total lease

expense. This guidance is effective for annual and interim reporting periods of public entities beginning after December 15, 2018. Therefore, we will adopt the standard in the first quarter of 2019. We are in the process of evaluating the effect of the adoption of ASU 2016-02 on our consolidated financial statements. We believe the recognition of right-of-use assets and lease liabilities will result in material increases in assets and liabilities reflected on our consolidated balance sheets. We do not expect the adoption of ASU 2016-02 to have a material impact on our consolidated statements of operations and cash flows.

Adoption of New Accounting Standards: ASU 2014-09, Revenue - Revenue from Contracts with Customers. On January 1, 2018, we adopted ASU 2014-09 and all the related amendments, (collectively, “ASC 606”) using the modified retrospective method. Under this method, a cumulative effect of initially applying the new revenue standard requires an adjustment to the opening balance of retained earnings, and the comparative information continues to be reported under the accounting standards in effect for those periods prior to adoption. The cumulative effect of initially applying the new standard was not material to our consolidated financial statements. We do not expect the adoption of this guidance to have a material effect on our results of operations in future periods.

ASU 2017-12, Accounting for Derivatives and Hedging Transactions (Topic 815) Targeted Improvements to Accounting for Hedging Activities. In March 2018, we early adopted ASU 2017-12. The new standard amends the hedge accounting model to better portray an organization’s risk management activities in the financial statements, as well as simplifies the applications of certain hedge accounting guidance. The implementation of ASU 2017-12 did not have a material impact on our consolidated financial statements.

NOTE 2 – REVENUE RECOGNITION

Revenue is recognized when control of promised goods or services is transferred to our customers in an amount that reflects the consideration to which we expect to be entitled in exchange for those goods or services. Substantially all of our revenue is recognized when products are shipped or delivered to our customers, and payment is due from our customers at the time of billing with a majority of our customers having 30-day terms. Returns are estimated and recorded as a reduction of revenue. Amounts received in advance of shipment are deferred and recognized when the performance obligations are satisfied. Sales taxes collected from customers and remitted to governmental authorities are accounted for on a net basis and, therefore, are

Table Of Contents

excluded from sales in the accompanying consolidated statements of operations. Cost of sales includes the cost of inventory sold and related items, such as vendor rebates, inventory allowances and reserves, and shipping and handling costs associated with inbound and outbound freight, as well as depreciation and amortization and amortization of intangible assets. In some cases, particularly with third party pipe shipments, shipping and handling costs are considered separate performance obligations, and as such, the revenue and cost of sales are recorded when the performance obligation is fulfilled.

Our contracts with customers ordinarily involve performance obligations that are one year or less. Therefore, we have applied ASC 606's optional exemption that permits the omission of information about our unfulfilled performance obligations as of the balance sheet dates.

Contract Balances: Variations in the timing of revenue recognition, invoicing and receipt of payment result in categories of assets and liabilities that include invoiced accounts receivable, uninvoiced accounts receivable, contract assets and deferred revenue (contract liabilities) on the consolidated balance sheets.

Generally, revenue recognition and invoicing occur simultaneously as we transfer control of promised goods or services to our customers. We consider contract assets to be accounts receivable when we have an unconditional right to consideration and only the passage of time is required before payment is due. In certain cases, particularly those involving customer-specific documentation requirements, invoicing is delayed until we are able to meet the documentation requirements. In these cases, we recognize a contract asset separate from accounts receivable until those requirements are met, and we are able to invoice the customer. Our contract asset balance associated with these requirements, as of June 30, 2018 and December 31, 2017, was \$36 million and \$31 million, respectively. These contract asset balances are included within accounts receivable in the accompanying consolidated balance sheets.

We record contract liabilities, or deferred revenue, when cash payments are received from customers in advance of our performance, including amounts which are refundable. The deferred revenue balance at June 30, 2018 and December 31, 2017 was \$31 million and \$30 million, respectively. During the six months ended June 30, 2018, we recognized \$1 million of revenue that was deferred as of December 31, 2017. Deferred revenue balances are included within accrued expenses and other current liabilities in the accompanying consolidated balance sheets.

Disaggregated Revenue: Our disaggregated revenue represents our business of selling PVF to the energy sector across each of the upstream (exploration, production and extraction of underground oil and gas), midstream (gathering and transmission of oil and gas, gas utilities, and the storage and distribution of oil and gas) and downstream (crude oil refining and petrochemical and chemical processing and general industrials) markets in each of our reportable segments. Each of our end markets and geographical reportable segments are impacted and influenced by varying factors, including macroeconomic environment, commodity prices, maintenance and capital spending, and exploration and production activity. As such, we believe that this information is important in depicting the nature, amount, timing and uncertainty of our contracts with customers.

The following table presents our revenue disaggregated by revenue source (in millions):

Three Months Ended
June 30,

| | U.S. | Canada | International | Total |
|------------|--------|--------|---------------|----------|
| 2018: | | | | |
| Upstream | \$ 189 | \$ 64 | \$ 54 | \$ 307 |
| Midstream | 454 | 8 | 10 | 472 |
| Downstream | 235 | 8 | 60 | 303 |
| | \$ 878 | \$ 80 | \$ 124 | \$ 1,082 |
| 2017: | | | | |
| Upstream | \$ 159 | \$ 50 | \$ 49 | \$ 258 |
| Midstream | 379 | 14 | 27 | 420 |
| Downstream | 182 | 5 | 57 | 244 |
| | \$ 720 | \$ 69 | \$ 133 | \$ 922 |

Table Of Contents

Six Months Ended
June 30,

| | U.S. | Canada | International | Total |
|------------|----------|--------|---------------|----------|
| 2018: | | | | |
| Upstream | \$ 367 | \$ 121 | \$ 121 | \$ 609 |
| Midstream | 847 | 22 | 13 | 882 |
| Downstream | 470 | 15 | 116 | 601 |
| | \$ 1,684 | \$ 158 | \$ 250 | \$ 2,092 |
| 2017: | | | | |
| Upstream | \$ 299 | \$ 111 | \$ 93 | \$ 503 |
| Midstream | 725 | 25 | 41 | 791 |
| Downstream | 362 | 10 | 118 | 490 |
| | \$ 1,386 | \$ 146 | \$ 252 | \$ 1,784 |

NOTE 3 – INVENTORIES

The composition of our inventory is as follows (in millions):

| | June 30, 2018 | December 31, 2017 |
|--|------------------|-------------------------|
| Finished goods inventory at average cost: | | |
| Valves, automation, measurement and instrumentation | \$ 331 | \$ 292 |
| Carbon steel pipe, fittings and flanges | 355 | 268 |
| All other products | 337 | 270 |
| | 1,023 | 830 |
| Less: Excess of average cost over LIFO cost (LIFO reserve) | (117) | (95) |
| Less: Other inventory reserves | (34) | (34) |
| | \$ 872 | \$ 701 |

NOTE 4 – LONG-TERM DEBT

The components of our long-term debt are as follows (in millions):

| | June 30, 2018 | December 31, 2017 |
|---|---------------------|-------------------------|
| Senior Secured Term Loan B, net of discount and issuance costs of \$3 | \$ 395 | \$ 397 |
| Global ABL Facility | 313 | 129 |
| | 708 | 526 |
| Less: current portion | 4 | 4 |
| | \$ 704 | \$ 522 |

Senior Secured Term Loan B: We have a seven-year Senior Secured Term Loan B (the “Term Loan”) with an original principal amount of \$400 million, which amortizes in equal quarterly installments of 1% per year with the balance payable in September 2024, when the facility matures. The Term Loan allows for incremental increases in facility size by up to an aggregate of \$200 million, plus an additional amount such that the Company’s first lien leverage ratio (as defined under the Term Loan) would not exceed 4.00 to 1.00. MRC Global (US) Inc. is the borrower under this facility, which is guaranteed by MRC Global Inc. as well as all of its wholly owned U.S. subsidiaries. In addition, it is secured by a second lien on the assets securing our Global ABL Facility, defined below, (which includes accounts receivable, inventory and related assets) and a first

Table Of Contents

lien on substantially all of the other assets of MRC Global Inc. and those of its U.S. subsidiaries, as well as a pledge of all of the capital stock of our domestic subsidiaries and 65% of the capital stock of first tier, non-U.S. subsidiaries. We are required to repay the Term Loan with certain asset sales and insurance proceeds, certain debt proceeds and 50% of excess cash flow, as defined in the Term Loan, (reducing to 25% if our first lien leverage ratio is no more than 2.75 to 1.00 and 0% if our first lien leverage ratio is no more than 2.50 to 1.00). In addition, the Term Loan contains a number of customary restrictive covenants.

In May 2018, the Company entered into Refinancing Amendment No. 2 relating to the Term Loan. Pursuant to this amendment, the Company and the other parties thereto agreed to reduce the interest rate margin applicable to term loans, in the case of loans incurring interest based on the base rate, from 250 basis points to 200 basis points, and in the case of loans incurring interest based on LIBOR, from 350 basis points to 300 basis points. The parties to the amendment also agreed to reduce the base rate ‘floor’ from 2.00% to 1.00% and to reduce the LIBOR ‘floor’ from 1.00% to 0.00%. The parties also reset the prepayment premium applicable to voluntary prepayments of the term loans such that repayments made in connection with certain re-pricing transactions will be subject to a 1% premium if made during the first six-months following the date of the amendment. Except as described above, the terms of the Term Loan Agreement generally were not modified as a result of the amendment.

Global ABL Facility: We have an \$800 million multi-currency asset-based revolving credit (the “Global ABL Facility”) that matures in September 2022. This facility is comprised of \$675 million in revolver commitments in the United States, \$65 million in Canada, \$18 million in Norway, \$15 million in Australia, \$13 million in the Netherlands, \$7 million in the United Kingdom and \$7 million in Belgium. It contains an accordion feature that allows us to increase the principal amount of the facility by up to \$200 million, subject to securing additional lender commitments. MRC Global Inc. and each of its current and future wholly owned material U.S. subsidiaries guarantee the obligations of our borrower subsidiaries under the Global ABL Facility. Additionally, each of our non-U.S. borrower subsidiaries guarantees the obligations of our other non-U.S. borrower subsidiaries under the Global ABL Facility. Outstanding obligations are generally secured by a first priority security interest in accounts receivable, inventory and related assets. Excess Availability, as defined under our Global ABL Facility, was \$414 million as of June 30, 2018.

Interest on Borrowings: The interest rates on our borrowings outstanding at June 30, 2018 and December 31, 2017, including a floating to fixed interest rate swap and amortization of debt issuance costs, were as set forth below. On a comparable basis, the weighted average interest rate at March 31, 2018 was 5.15%.

| | June 30, 2018 | December 31, 2017 |
|--------------------------------|------------------|-------------------------|
| Senior Secured Term Loan B | 5.60% | 5.18% |
| Global ABL Facility | 3.77% | 3.19% |
| Weighted average interest rate | 4.79% | 4.69% |

NOTE 5 – INCOME TAXES

For interim periods, our income tax expense is computed based upon our estimated annual effective tax rate and any discrete items that impact the interim periods. Our effective tax rates for the three and six months ended June 30, 2018 were each 27% and for the three and six months ended June 30, 2017 were 33% and 25%, respectively. Our rates generally differ from the U.S. federal statutory rates of 21% and 35% for the six months ended June 30, 2018 and 2017, respectively, as a result of state income taxes and differing foreign income tax rates. The 2018 effective tax rate exceeds the U.S. statutory rate primarily as a result of pre-tax losses in certain foreign jurisdictions with no corresponding tax benefit. The 2017 effective tax rate was below the U.S. statutory rate as a result of a benefit related to the foreign currency exchanges losses and the adoption of ASU 2016-09, Compensation – Stock Compensation, which resulted in a discrete tax benefit of \$2 million related to the vesting of stock awards.

As of December 31, 2017, we recorded provisional tax estimates associated with the passage of the Tax Cuts and Jobs Act of 2017 (the “Tax Act”). These provisional amounts included a \$57 million benefit for the re-measurement of deferred tax assets and liabilities and a \$7 million transition tax expense related to undistributed foreign earnings. In accordance with the Securities and Exchange Commission’s Staff Accounting Bulletin No. 118 (“SAB 118”), these provisional amounts will be finalized during 2018. Any adjustments required to the provisional amounts will be reflected in income tax expense in the period the adjustment is identified.

Table Of Contents

NOTE 6 – REDEEMABLE PREFERRED STOCK

Preferred Stock Issuance

In June 2015, we issued 363,000 shares of Series A Convertible Perpetual Preferred Stock (the “Preferred Stock”) and received proceeds of \$355 million, net of transaction fees. The Preferred Stock ranks senior to our common stock with respect to dividend rights and rights on liquidation, winding-up and dissolution. The Preferred Stock has a stated value of \$1,000 per share, and holders of Preferred Stock are entitled to cumulative dividends payable quarterly in cash at a rate of 6.50% per annum. Holders of Preferred Stock are entitled to vote together with the holders of the common stock as a single class, in each case, on an as-converted basis, except where a separate class vote of the common stockholders is required by law. Holders of Preferred Stock have certain limited special approval rights, including with respect to the issuance of pari passu or senior equity securities of the Company.

The Preferred Stock is convertible at the option of the holders into shares of common stock at an initial conversion rate of 55.9284 shares of common stock for each share of Preferred Stock, which represents an initial conversion price of \$17.88 per share of common stock, subject to adjustment. On or after the fifth anniversary of the initial issuance of the Preferred Stock, the Company will have the option to redeem, in whole but not in part, all the outstanding shares of Preferred Stock at 105% of par value, subject to certain redemption price adjustments on the basis of the date of the conversion. After the seventh anniversary of the initial issuance of Preferred Stock, the Company will have the option to redeem all of the outstanding shares of Preferred Stock at par value. We may elect to convert the Preferred Stock, in whole but not in part, into the relevant number of shares of common stock on or after the 54th month after the initial issuance of the Preferred Stock if the last reported sale price of the common stock has been at least 150% of the conversion price then in effect for a specified period. The conversion rate is subject to customary anti-dilution and other adjustments.

Holders of the Preferred Stock may, at their option, require the Company to repurchase their shares in the event of a fundamental change, as defined in the agreement. The repurchase price is based on the original \$1,000 per share purchase price except in the case of a liquidation in which case they would receive the greater of \$1,000 per share and the amount that would be received if they held common stock converted at the conversion rate in effect at the time of the fundamental change. Because this feature could require redemption as a result of the occurrence of an event not solely within the control of the Company, the Preferred Stock is classified as temporary equity on our balance sheet.

NOTE 7 – STOCKHOLDERS’ EQUITY

Share Repurchase Program

In November 2015, the Company’s board of directors authorized a share repurchase program for common stock up to \$100 million, which was increased in November 2016 to \$125 million. In the first quarter of 2017, the Company completed the repurchase of all shares authorized under the program.

In October 2017, the Company’s board of directors authorized a new share repurchase program for common stock of up to \$100 million. In the second quarter of 2018, the Company completed the repurchases of all shares authorized under this program.

Summary of share repurchase activity under the repurchase program:

| | Three Months Ended | | Six Months Ended | |
|--|--------------------|---------------|------------------|---------------|
| | June 30, 2018 | June 30, 2017 | June 30, 2018 | June 30, 2017 |
| Number of shares acquired on the open market | 1,144,379 | - | 2,871,204 | 859,830 |
| Average price per share | \$ 17.39 | \$ - | \$ 17.39 | \$ 20.54 |
| Total cost of acquired shares (in millions) | \$ 20 | \$ - | \$ 50 | \$ 18 |

In total, under both programs, we have acquired 14,622,930 shares at an average price per share of \$15.38 for a total cost of \$225 million. There were 90,300,790 shares of common stock outstanding as of June 30, 2018.

Equity Compensation Plans

Our 2011 Omnibus Incentive Plan originally had 3,250,000 shares reserved for issuance under the plan. In April 2015, our shareholders approved an additional 4,250,000 shares for reservation for issuance under the plan. The plan permits the issuance

Table Of Contents

of stock options, stock appreciation rights, restricted stock, restricted stock units, performance shares, performance units and other stock-based and cash-based awards. Since the adoption of the 2011 Omnibus Incentive Plan, the Company's Board of Directors has periodically granted stock options, restricted stock awards, restricted stock units and performance share units to directors and employees. Options and stock appreciation rights may not be granted at prices less than the fair market value of our common stock on the date of the grant, nor for a term exceeding ten years. For employees, vesting generally occurs over a three to five year period on the anniversaries of the date specified in the employees' respective stock option, restricted stock award, restricted stock unit and performance share unit award agreements, subject to accelerated vesting under certain circumstances set forth in the agreements. Vesting for directors generally occurs on the one-year anniversary of the grant date. In 2018, 222,435 performance share unit awards, 505,297 shares of restricted stock units and 81,542 shares of restricted stock have been granted to employees and members of our board of directors. To date, since the plan's inception in 2011, before consideration of forfeitures, 6,680,204 shares have been granted to management, members of our board of directors and key employees under this plan. A Black-Scholes option-pricing model is used to estimate the fair value of the stock options. A Monte Carlo simulation is completed to estimate the fair value of performance share unit awards with a stock price performance component. We expense the fair value of all equity grants, including performance share unit awards, on a straight-line basis over the vesting period.

Accumulated Other Comprehensive Loss

Accumulated other comprehensive loss in the accompanying consolidated balance sheets consists of the following (in millions):

| | June 30, 2018 | December 31, 2017 |
|--------------------------------------|---------------------|-------------------------|
| Currency translation adjustments | \$ (219) | \$ (209) |
| Pension related adjustments | (1) | (1) |
| Accumulated other comprehensive loss | \$ (220) | \$ (210) |

Earnings per Share

Earnings per share are calculated in the table below (in millions, except per share amounts).

| | Three Months Ended | | Six Months Ended | |
|--|-----------------------|---------------------|---------------------|---------------------|
| | June 30, 2018 | June 30, 2017 | June 30, 2018 | June 30, 2017 |
| Net income | \$ 22 | \$ 6 | \$ 40 | \$ 12 |
| Less: Dividends on Series A Preferred Stock | 6 | 6 | 12 | 12 |
| Net income attributable to common stockholders | \$ 16 | \$ - | \$ 28 | \$ - |

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| | | | | |
|---|------|------|------|------|
| Weighted average basic shares outstanding | 90.1 | 94.5 | 90.7 | 94.6 |
| Effect of dilutive securities | 1.5 | 1.1 | 2.0 | 1.4 |
| Weighted average diluted shares outstanding | 91.6 | 95.6 | 92.7 | 96.0 |

Net income per share:

| | | | | |
|---------|---------|------|---------|------|
| Basic | \$ 0.18 | \$ - | \$ 0.31 | \$ - |
| Diluted | \$ 0.17 | \$ - | \$ 0.30 | \$ - |

Equity awards and shares of Preferred Stock are disregarded in the calculation of diluted earnings per share if they are determined to be anti-dilutive. For the three and six months ended June 30, 2018 and June 30, 2017 all of the shares of the Preferred Stock were anti-dilutive. For the three and six months ended June 30, 2018, we had approximately 3.2 million and 3.5 million anti-dilutive stock options, respectively. For the three and six months ended June 30, 2017, we had approximately 2.1 million anti-dilutive stock options. There were no anti-dilutive restricted stock, restricted units or performance stock unit awards for the three and six months ended June 30, 2018 and 2017.

NOTE 8 – SEGMENT INFORMATION

Our business is comprised of four operating segments: U.S. Eastern Region and Gulf Coast, U.S. Western Region, Canada and International. Our International segment consists of our operations outside of the U.S. and Canada. These segments represent

Table Of Contents

our business of selling PVF to the energy sector across each of the upstream (exploration, production and extraction of underground oil and gas), midstream (gathering and transmission of oil and gas, gas utilities, and the storage and distribution of oil and gas) and downstream (crude oil refining and petrochemical and chemical processing and general industrials) markets. Our two U.S. operating segments have been aggregated into a single reportable segment based on their economic similarities. As a result, we report segment information for the U.S., Canada and International.

The following table presents financial information for each reportable segment (in millions):

| | Three Months Ended | | Six Months Ended | |
|----------------------------|--------------------|---------------|------------------|---------------|
| | June 30, 2018 | June 30, 2017 | June 30, 2018 | June 30, 2017 |
| Sales | | | | |
| U.S. | \$ 878 | \$ 720 | \$ 1,684 | \$ 1,386 |
| Canada | 80 | 69 | 158 | 146 |
| International | 124 | 133 | 250 | 252 |
| Consolidated sales | \$ 1,082 | \$ 922 | \$ 2,092 | \$ 1,784 |
| Operating income | | | | |
| U.S. | \$ 37 | \$ 21 | \$ 65 | \$ 32 |
| Canada | 2 | 1 | 4 | 4 |
| International | 2 | (5) | 3 | (5) |
| Total operating income | 41 | 17 | 72 | 31 |
| Interest expense | (10) | (8) | (18) | (15) |
| Other, net | (1) | - | 1 | - |
| Income before income taxes | \$ 30 | \$ 9 | \$ 55 | \$ 16 |
| | | | | |
| | | | December | |
| | | | June 30, | 31, |
| | | | 2018 | 2017 |
| Total assets | | | | |
| U.S. | | | \$ 2,244 | \$ 1,970 |
| Canada | | | 152 | 162 |
| International | | | 220 | 208 |
| Total assets | | | \$ 2,616 | \$ 2,340 |

Our sales by product line are as follows (in millions):

| Type | Three Months Ended | | Six Months Ended | |
|---|--------------------|-------------------|------------------|-------------------|
| | June 30, 2018 | June 30, 2017 (1) | June 30, 2018 | June 30, 2017 (1) |
| Line pipe | \$ 212 | \$ 170 | \$ 370 | \$ 316 |
| Carbon steel fittings and flanges | 178 | 139 | 349 | 262 |
| Total carbon steel pipe, fittings and flanges | 390 | 309 | 719 | 578 |
| Valves, automation, measurement and instrumentation | 375 | 327 | 753 | 649 |
| Gas products | 147 | 125 | 271 | 241 |
| Stainless steel and alloy pipe and fittings | 49 | 50 | 102 | 91 |
| General oilfield products | 121 | 111 | 247 | 225 |
| | \$ 1,082 | \$ 922 | \$ 2,092 | \$ 1,784 |

(1) \$18 million of sales for the three months ended June 30, 2017 and \$36 million of sales for the six months ended June 30, 2017 have been reclassified from gas products to general oilfield products to conform with the current year presentation.

Table Of Contents

NOTE 9 – FAIR VALUE MEASUREMENTS

From time to time, we use derivative financial instruments to help manage our exposure to interest rate risk and fluctuations in foreign currencies.

Interest Rate Swap: In March 2018, we entered into a five-year interest rate swap that became effective on March 31, 2018, with a notional amount of \$250 million from which the Company will receive payments at 1-month LIBOR and make monthly payments at a fixed rate of 2.7145% with settlement and reset dates on or near the last business day of each month until maturity. The fair value of the swap at inception was zero.

We have designated the interest rate swap as an effective cash flow hedge utilizing the guidance under ASU 2017-12. As such, the valuation of the interest rate swap is recorded as an asset or liability, and the gain or loss on the derivative is recorded as a component of other comprehensive income. Interest rate swap agreements are reported at fair value utilizing Level 2 inputs. We obtain dealer quotations to value our interest rate swap agreements. The fair value of our interest rate swap is estimated based on the present value of the difference between expected cash flows calculated at the contracted interest rates and the expected cash flows at current market interest rates. We recognize interest rate swaps on the accompanying balance sheet at fair value using observable inputs such as yield curves and other market-based factors. The fair value of the interest rate swap was \$0 million as of June 30, 2018.

Foreign Exchange Forward and Option Contracts: Foreign exchange forward contracts are reported at fair value utilizing Level 2 inputs, as the fair value is based on broker quotes for the same or similar derivative instruments. Our foreign exchange derivative instruments are freestanding and, accordingly, changes in their fair market value are recorded in earnings. The total notional amount of our forward foreign exchange contracts and options was approximately \$32 million and \$60 million at June 30, 2018 and December 31, 2017, respectively. We had approximately \$0 million recorded as liabilities on our consolidated balance sheets as of June 30, 2018 and December 31, 2017.

With the exception of long-term debt, the fair values of our financial instruments, including cash and cash equivalents, accounts receivable, trade accounts payable and accrued liabilities approximate carrying value. The carrying value of our debt was \$708 million and \$526 million at June 30, 2018 and December 31, 2017, respectively. We estimate the fair value of the Term Loan using Level 2 inputs, or quoted market prices. The fair value of our debt was \$712 million and \$533 million at June 30, 2018 and December 31, 2017 respectively.

NOTE 10 – COMMITMENTS AND CONTINGENCIES

Litigation

Asbestos Claims. We are one of many defendants in lawsuits that plaintiffs have brought seeking damages for personal injuries that exposure to asbestos allegedly caused. Plaintiffs and their family members have brought these lawsuits against a large volume of defendant entities as a result of the defendants' manufacture, distribution, supply or other involvement with asbestos, asbestos containing-products or equipment or activities that allegedly caused plaintiffs to be exposed to asbestos. These plaintiffs typically assert exposure to asbestos as a consequence of third-party manufactured products that our MRC Global (US) Inc. subsidiary purportedly distributed. As of June 30, 2018, we are named a defendant in approximately 552 lawsuits involving approximately 1,152 claims. No asbestos lawsuit has resulted in a judgment against us to date, with a majority being settled, dismissed or otherwise resolved. Applicable third-party insurance has substantially covered these claims, and insurance should continue to cover a substantial majority of existing and anticipated future claims. Accordingly, we have recorded a liability for our estimate of the most likely settlement of asserted claims and a related receivable from insurers for our estimated recovery, to the extent we believe that the amounts of recovery are probable. It is not possible to predict the outcome of these claims and proceedings. However, in our opinion, the likelihood that the ultimate disposition of any of these claims and legal proceedings will have a material adverse effect on our consolidated financial statements is remote.

Other Legal Claims and Proceedings. From time to time, we have been subject to various claims and involved in legal proceedings incidental to the nature of our businesses. We maintain insurance coverage to reduce financial risk associated with certain of these claims and proceedings. It is not possible to predict the outcome of these claims and proceedings. However, in our opinion, the likelihood that the ultimate disposition of any of these claims and legal proceedings will have a material adverse effect on our consolidated financial statements is remote.

Product Claims. From time to time, in the ordinary course of our business, our customers may claim that the products that we distribute are either defective or require repair or replacement under warranties that either we or the manufacturer may provide to the customer. These proceedings are, in the opinion of management, ordinary and routine matters incidental to our normal business. Our purchase orders with our suppliers generally require the manufacturer to indemnify us against any product liability claims, leaving the manufacturer ultimately responsible for these claims. In many cases, state, provincial or foreign

Table Of Contents

law provides protection to distributors for these sorts of claims, shifting the responsibility to the manufacturer. In some cases, we could be required to repair or replace the products for the benefit of our customer and seek our recovery from the manufacturer for our expense. In our opinion, the likelihood that the ultimate disposition of any of these claims and legal proceedings will have a material adverse effect on our consolidated financial statements is remote.

Customer Contracts

We have contracts and agreements with many of our customers that dictate certain terms of our sales arrangements (pricing, deliverables, etc.). While we make every effort to abide by the terms of these contracts, certain provisions are complex and often subject to varying interpretations. Under the terms of these contracts, our customers have the right to audit our adherence to the contract terms. Historically, any settlements that have resulted from these customer audits have not been material to our consolidated financial statements.

Purchase Commitments

We have purchase obligations consisting primarily of inventory purchases made in the normal course of business to meet operating needs. While our vendors often allow us to cancel these purchase orders without penalty, in certain cases, cancellations may subject us to cancellation fees or penalties depending on the terms of the contract.

Table Of Contents

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

You should read the following discussion and analysis of our financial condition and results of operations in conjunction with our financial statements and related notes included elsewhere in this report. This discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions. As used in this Form 10-Q, unless otherwise indicated or the context otherwise requires, all references to the "Company," "MRC Global," "we," "our" or "us" refer to MRC Global Inc. and its consolidated subsidiaries.

Cautionary Note Regarding Forward-Looking Statements

Management's Discussion and Analysis of Financial Condition and Results of Operations (as well as other sections of this Quarterly Report on Form 10-Q) contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Forward-looking statements include those preceded by, followed by or including the words "will," "expect," "intended," "anticipated," "believe," "project," "forecast," "propose," "plan," "estimate," "enable," and other expressions, including, for example, statements about our business strategy, our industry, our future profitability, growth in the industry sectors we serve, our expectations, beliefs, plans, strategies, objectives, prospects and assumptions, and estimates and projections of future activity and trends in the oil and natural gas industry. These forward-looking statements are not guarantees of future performance. These statements are based on management's expectations that involve a number of business risks and uncertainties, any of which could cause actual results to differ materially from those expressed in or implied by the forward-looking statements. These statements involve known and unknown risks, uncertainties and other factors, most of which are difficult to predict and many of which are beyond our control, including the factors described under "Risk Factors," that may cause our actual results and performance to be materially different from any future results or performance expressed or implied by these forward-looking statements. Such risks and uncertainties include, among other things:

- decreases in oil and natural gas prices;
- decreases in oil and natural gas industry expenditure levels, which may result from decreased oil and natural gas prices or other factors;
- increased usage of alternative fuels, which may negatively affect oil and natural gas industry expenditure levels;
- U.S. and international general economic conditions;
- our ability to compete successfully with other companies in our industry;
- the risk that manufacturers of the products we distribute will sell a substantial amount of goods directly to end users in the industry sectors we serve;
- unexpected supply shortages;
- cost increases by our suppliers;
- our lack of long-term contracts with most of our suppliers;

- suppliers' price reductions of products that we sell, which could cause the value of our inventory to decline;
- decreases in steel prices, which could significantly lower our profit;
- increases in steel prices, which we may be unable to pass along to our customers which could significantly lower our profit;
- our lack of long-term contracts with many of our customers and our lack of contracts with customers that require minimum purchase volumes;
- changes in our customer and product mix;
- risks related to our customers' creditworthiness;
- the success of our acquisition strategies;
- the potential adverse effects associated with integrating acquisitions into our business and whether these acquisitions will yield their intended benefits;
- our significant indebtedness;
- the dependence on our subsidiaries for cash to meet our obligations;
- changes in our credit profile;
- a decline in demand for or adverse change in the value of certain of the products we distribute if tariffs and duties on these products are imposed or lifted;
- environmental, health and safety laws and regulations and the interpretation or implementation thereof;

Table Of Contents

- the sufficiency of our insurance policies to cover losses, including liabilities arising from litigation;
- product liability claims against us;
- pending or future asbestos-related claims against us;
- the potential loss of key personnel;
- interruption in the proper functioning of our information systems;
- the occurrence of cybersecurity incidents;
- loss of third-party transportation providers;
- potential inability to obtain necessary capital;
- risks related to adverse weather events or natural disasters;
- impairment of our goodwill or other intangible assets;
- adverse changes in political or economic conditions in the countries in which we operate;
- exposure to U.S. and international laws and regulations, including the Foreign Corrupt Practices Act and the U.K. Bribery Act and other economic sanctions programs;
- risks associated with international instability and geopolitical developments;
- risks relating to ongoing evaluations of internal controls required by Section 404 of the Sarbanes-Oxley Act;
- our intention not to pay dividends; and
- risks related to changing laws and regulations.

Undue reliance should not be placed on our forward-looking statements. Although forward-looking statements reflect our good faith beliefs, reliance should not be placed on forward-looking statements because they involve known and unknown risks, uncertainties and other factors, which may cause our actual results, performance or achievements to differ materially from anticipated future results, performance or achievements expressed or implied by such forward-looking statements. We undertake no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events, changed circumstances or otherwise, except to the extent law requires.

Overview

We are the largest global industrial distributor, based on sales, of pipe, valves, and fittings (“PVF”) and related products and services to the energy industry and hold a leading position in our industry across each of the upstream (exploration, production and extraction of underground oil and natural gas), midstream (gathering and transmission of oil and natural gas, natural gas utilities and the storage and distribution of oil and natural gas) and downstream (crude oil refining, petrochemical and chemical processing and general industrials) sectors. Our business is segregated into three geographic reportable segments, consisting of our U.S., Canada and International operations. We serve our

customers from approximately 300 service locations. We offer a wide array of PVF and oilfield supplies encompassing a complete line of products from our global network of approximately 12,000 suppliers to our more than 16,000 customers. We are diversified by geography, the industry sectors we serve and the products we sell. We seek to provide best-in-class service to our customers by satisfying the most complex, multi-site needs of many of the largest companies in the energy sector as their primary PVF supplier. We believe the critical role we play in our customers' supply chain, together with our extensive product offering, broad global presence, customer-linked scalable information systems and efficient distribution capabilities, serve to solidify our long-standing customer relationships and drive our growth. As a result, we have an average relationship of over 25 years with our 25 largest customers.

Key Drivers of Our Business

Our revenue is predominantly derived from the sale of PVF and other oilfield and industrial supplies to the energy sector globally. Our business is therefore dependent upon both the current conditions and future prospects in the energy industry and, in particular, maintenance and expansionary operating and capital expenditures by our customers in the upstream, midstream and downstream sectors of the industry. Long-term growth in spending has been driven by several factors, including demand growth for petroleum and petroleum derived products, underinvestment in global energy infrastructure, growth in shale and unconventional exploration and production ("E&P") activity, and anticipated strength in the oil, natural gas, refined products and petrochemical sectors. The outlook for future oil, natural gas, refined products and petrochemical PVF spending is influenced by numerous factors, including the following:

- Oil and Natural Gas Prices. Sales of PVF and related products to the oil and natural gas industry constitute over 90% of our sales. As a result, we depend upon the oil and natural gas industry and its ability and willingness to make maintenance and capital expenditures to explore for, produce and process oil, natural gas and refined products. Oil and natural gas prices, both current and projected, along with the costs necessary to produce oil and

Table Of Contents

gas, impact other drivers of our business, including capital spending by customers, additions to and maintenance of pipelines, refinery utilization and petrochemical processing activity.

- **Economic Conditions.** The demand for the products we distribute is dependent on the general economy, the energy sector and other factors. Changes in the general economy or in the energy sector (domestically or internationally) can cause demand for the products we distribute to materially change.
- **Manufacturer and Distributor Inventory Levels of PVF and Related Products.** Manufacturer and distributor inventory levels of PVF and related products can change significantly from period to period. Increased inventory levels by manufacturers or other distributors can cause an oversupply of PVF and related products in the industry sectors we serve and reduce the prices that we are able to charge for the products we distribute. Reduced prices, in turn, would likely reduce our profitability. Conversely, decreased manufacturer inventory levels may ultimately lead to increased demand for our products and would likely result in increased sales volumes and overall profitability.
- **Steel Prices, Availability and Supply and Demand.** Fluctuations in steel prices can lead to volatility in the pricing of the products we distribute, especially carbon steel line pipe products, which can influence the buying patterns of our customers. A majority of the products we distribute contain various types of steel. The worldwide supply and demand for these products, or other steel products that we do not supply, impacts the pricing and availability of our products and, ultimately, our sales and operating profitability.

Recent Trends and Outlook

During the first six months of 2018, the average oil price of West Texas Intermediate (“WTI”) increased to \$65.55 per barrel from \$49.85 per barrel in the first six months of 2017. Natural gas prices decreased slightly to an average price of \$2.96/Mcf (Henry Hub) for the first six months of 2018 compared to \$3.05/Mcf (Henry Hub) for the first six months of 2017. North American drilling rig activity increased 16% in the first six months of 2018 as compared to the first six months of 2017. U.S. well completions were up 32% in the first six months of 2018 compared to the same period in 2017.

Following a dramatic two-year decline in E&P capital spending by our customers in 2015 and 2016, our business rebounded with 20% sales growth in 2017. We remain encouraged by stability in oil prices and sustained growth in drilling and completion activity. Prominent E&P spending surveys, which include many of our customers, indicate that 2018 spending will increase by a high single digit percentage globally including double digit growth in North America combined with more modest growth internationally. These positive macroeconomic variables combined with other favorable influences directly impact each of our business sectors. Healthy commodity prices and an emphasis on completing drilled but uncompleted wells (“DUCs”) benefits our upstream business. In addition, a more favorable regulatory environment in the United States has benefited our business, particularly in the midstream sector where we continue to see modernization and integrity projects in the gas utility space, as well as increased demand for take away capacity in oil and gas producing basins. Our domestic downstream sector has benefitted from the improved access to and stability in pricing of the necessary feedstocks available from increased, and in some cases, new upstream production. We expect these favorable business trends to continue throughout 2018 and into 2019.

In March 2018, the President of the United States signed a proclamation (“Section 232”) imposing a 25% tariff on all steel imports and 10% on all aluminum imports into the U.S. Section 232 impacts all carbon products, including pipe, fittings and flanges. Certain countries have been exempted from the provisions of Section 232, and in certain cases, a quota system rather than tariffs has been implemented. In July 2018, pursuant to Section 301 of the Trade Act of 1974 (“Section 301”), additional tariffs of 25% went into effect on certain Chinese goods, including valves, valve parts and

gaskets that we distribute. Although these actions generally cause the price we pay for products to increase, we are able to leverage long-standing relationships with our suppliers and the volume of our purchases to ensure we receive market competitive pricing. In addition, our contracts with customers generally allow us to react quickly to price increases through mechanisms that enable us to pass those increases along as they occur. These issues are dynamic and continue to evolve. The ultimate impact on our revenue and LIFO expense remains subject to uncertainty. We expect to see higher revenue due to these customer contract positions and higher LIFO expense for the products that we sell to the extent they are impacted by higher prices caused by the tariffs and quotas.

Table Of Contents

We determine backlog by the amount of unshipped customer orders, either specific or general in nature, which the customer may revise or cancel in certain instances. The table below details our backlog by segment (in millions):

| | June 30, 2018 | December 31, 2017 | June 30, 2017 |
|---------------|---------------------|-------------------------|---------------------|
| U.S. | \$ 530 | \$ 559 | \$ 564 |
| Canada | 54 | 40 | 34 |
| International | 244 | 233 | 229 |
| | \$ 828 | \$ 832 | \$ 827 |

Approximately 4%, 14%, and 21% of our June 30, 2018, December 31, 2017 and June 30, 2017 ending backlog, respectively, was associated with one customer in our U.S. segment. In addition, approximately 13% and 14% of our ending backlog for June 30, 2018 and December 31, 2017, respectively, was associated with one customer in our International segment. In each case, these are related to significant ongoing customer projects. There can be no assurance that the backlog amounts will ultimately be realized as revenue or that we will earn a profit on the backlog of orders, but we expect that substantially all of the sales in our backlog will be realized in the next twelve months.

The following table shows key industry indicators for the three and six months ended June 30, 2018 and 2017:

| | Three Months Ended | | Six Months Ended | |
|---------------------------------------|--------------------|------------------|------------------|------------------|
| | June 30, 2018 | June 30, 2017 | June 30, 2018 | June 30, 2017 |
| Average Rig Count (1): | | | | |
| United States | 1,039 | 895 | 1,003 | 819 |
| Canada | 108 | 117 | 188 | 206 |
| Total North America | 1,147 | 1,012 | 1,191 | 1,025 |
| International | 968 | 958 | 969 | 948 |
| Total | 2,115 | 1,970 | 2,160 | 1,973 |
| Average Commodity Prices (2): | | | | |
| WTI crude oil (per barrel) | \$ 68.07 | \$ 48.10 | \$ 65.55 | \$ 49.85 |
| Brent crude oil (per barrel) | \$ 74.53 | \$ 49.55 | \$ 70.67 | \$ 51.57 |
| Natural gas (\$/Mcf) | \$ 2.85 | \$ 3.08 | \$ 2.96 | \$ 3.05 |
| Average Monthly U.S. Well Permits (3) | | | | |
| U.S. Wells Completed (2) | 4,709 | 3,482 | 4,656 | 3,391 |
| 3:2:1 Crack Spread (4) | \$ 21.06 | \$ 17.04 | \$ 19.38 | \$ 16.38 |

(1) Source-Baker Hughes (www.bhge.com) (Total rig count includes oil, natural gas and other rigs.)

(2) Source-Department of Energy, EIA (www.eia.gov) (As revised)

(3) Source-Rig Data (U.S.)

(4) Source- Bloomberg

Table Of Contents

Results of Operations

Three Months Ended June 30, 2018 Compared to the Three Months Ended June 30, 2017

The breakdown of our sales by sector for the three months ended June 30, 2018 and 2017 was as follows (in millions):

| | Three Months Ended | | | |
|------------|--------------------|------|---------------|------|
| | June 30, 2018 | | June 30, 2017 | |
| Upstream | \$ 307 | 28% | \$ 258 | 28% |
| Midstream | 472 | 44% | 420 | 46% |
| Downstream | 303 | 28% | 244 | 26% |
| | \$ 1,082 | 100% | \$ 922 | 100% |

For the three months ended June 30, 2018 and 2017, the following table summarizes our results of operations (in millions):

| | Three Months Ended | | | |
|--|--------------------|---------------|-----------|----------|
| | June 30, 2018 | June 30, 2017 | \$ Change | % Change |
| Sales: | | | | |
| U.S. | \$ 878 | \$ 720 | \$ 158 | 22% |
| Canada | 80 | 69 | 11 | 16% |
| International | 124 | 133 | (9) | (7%) |
| Consolidated | \$ 1,082 | \$ 922 | \$ 160 | 17% |
| Operating income: | | | | |
| U.S. | \$ 37 | \$ 21 | \$ 16 | 76% |
| Canada | 2 | 1 | 1 | N/M |
| International | 2 | (5) | 7 | N/M |
| Consolidated | 41 | 17 | 24 | N/M |
| Interest expense | (10) | (8) | (2) | 25% |
| Other expense | (1) | - | (1) | N/M |
| Income tax expense | (8) | (3) | (5) | N/M |
| Net income | 22 | 6 | 16 | N/M |
| Series A preferred stock dividends | 6 | 6 | - | N/M |
| Net income attributable to common stockholders | \$ 16 | \$ - | \$ 16 | N/M |
| Gross profit | \$ 177 | \$ 149 | \$ 28 | 19% |
| Adjusted Gross Profit (1) | \$ 209 | \$ 171 | \$ 38 | 22% |
| Adjusted EBITDA (1) | \$ 78 | \$ 44 | \$ 34 | 77% |
| (1) | | | | |

Adjusted Gross Profit and Adjusted EBITDA are non-GAAP financial measures. For a reconciliation of these measures to an equivalent GAAP measure, see pages 19-21 herein.

Sales. Sales reflect consideration we are entitled to for goods and services when control of those goods and services is transferred to our customers. Our sales were \$1,082 million for the three months ended June 30, 2018 as compared to \$922 million for the three months ended June 30, 2017, an increase of \$160 million, or 17%. The strengthening of foreign currencies in areas where we operate outside of the U.S. dollar favorably impacted sales by \$9 million, or 1%.

U.S. Segment—Our U.S. sales increased to \$878 million for the three months ended June 30, 2018 from \$720 million for the three months ended June 30, 2017. This \$158 million, or 22%, increase reflected a \$30 million increase in the upstream sector, a \$75 million increase in the midstream sector, and a \$53 million increase in the downstream sector. The increase in the midstream sector is related to increased activity in the gas utility and transmission and gathering subsectors with several of our

Table Of Contents

customers, and the increase in the upstream sector is related to the increase in rig count and well completions. The increase in the downstream sector is primarily related to increased project work, turnaround activity and growth from new contracts.

Canada Segment—Our Canada sales increased to \$80 million for the three months ended June 30, 2018 from \$69 million for the three months ended June 30, 2017, an increase of \$11 million, or 16%. Canadian sales were favorably impacted by \$3 million, or 4%, as a result of the stronger Canadian dollar relative to the U.S. dollar.

International Segment—Our International sales decreased to \$124 million for the three months ended June 30, 2018 from \$133 million for the same period in 2017. The \$9 million, or 7%, decrease was primarily due to a \$17 million decrease in the midstream business related to an Australian line pipe project from 2017 with no such project work in the second quarter of 2018, offset by a \$5 million increase in upstream business related to project activity in Kazakhstan. The strengthening of foreign currencies in areas where we operate outside of the U.S. dollar favorably impacted sales by \$6 million, or 5%.

Gross Profit. Our gross profit was \$177 million (16.4% of sales) for the three months ended June 30, 2018 as compared to \$149 million (16.2% of sales) for the three months ended June 30, 2017. The \$28 million increase was primarily attributable to the increase in sales volumes. Our last-in, first-out (“LIFO”) inventory costing methodology resulted in an increase in cost of sales, as compared to average cost, of \$15 million and \$5 million in the second quarter of 2018 and 2017, respectively. Excluding the impact of LIFO, gross profit percentage improved by 100 basis points. While the second quarter of 2018 included a comparable level of major project sales as the second quarter of 2017, we benefited from a lower mix of lower margin line pipe sales. This combined with a favorable inflationary pricing environment drove the 100 basis point improvement in gross margins.

Adjusted Gross Profit. Adjusted Gross Profit increased to \$209 million (19.3% of sales) for the three months ended June 30, 2018 from \$171 million (18.5% of sales) for the three months ended June 30, 2017, an increase of \$38 million. Adjusted Gross Profit is a non-GAAP financial measure. We define Adjusted Gross Profit as sales, less cost of sales, plus depreciation and amortization, plus amortization of intangibles, and plus or minus the impact of our LIFO inventory costing methodology. We present Adjusted Gross Profit because we believe it is a useful indicator of our operating performance without regard to items, such as amortization of intangibles, that can vary substantially from company to company depending upon the nature and extent of acquisitions. Similarly, the impact of the LIFO inventory costing method can cause results to vary substantially from company to company depending upon whether they elect to utilize LIFO and depending upon which method they may elect. We use Adjusted Gross Profit as a key performance indicator in managing our business. We believe that gross profit is the financial measure calculated and presented in accordance with U.S. generally accepted accounting principles that is most directly comparable to Adjusted Gross Profit.

The following table reconciles Adjusted Gross Profit, a non-GAAP financial measure, with gross profit, as derived from our financial statements (in millions):

| Three Months Ended | Percentage | Percentage |
|--------------------|------------|------------|
|--------------------|------------|------------|

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| | June 30, 2018 | of Revenue* | June 30, 2017 | of Revenue* |
|-------------------------------|---------------------|-------------|---------------------|-------------|
| Gross profit, as reported | \$ 177 | 16.4% | \$ 149 | 16.2% |
| Depreciation and amortization | 6 | 0.6% | 6 | 0.7% |
| Amortization of intangibles | 11 | 1.0% | 11 | 1.2% |
| Increase in LIFO reserve | 15 | 1.4% | 5 | 0.5% |
| Adjusted Gross Profit | \$ 209 | 19.3% | \$ 171 | 18.5% |

*Does not foot due to rounding.

Selling, General and Administrative (“SG&A”) Expenses. Costs such as salaries, wages, employee benefits, rent, utilities, communications, insurance, fuel and taxes (other than state and federal income taxes) that are necessary to operate our branch and corporate operations are included in SG&A. Also contained in this category are certain items that are nonoperational in nature, including certain costs of acquiring and integrating other businesses. Our SG&A expenses were \$136 million for the three months ended June 30, 2018 as compared to \$132 million for the three months ended June 30, 2017. The \$4 million increase in SG&A is primarily related to an increase in employee-related costs, including wage and incentive increases following three years of wage freezes and incentive reductions as a result of the downturn in our business offset by the late 2017 reductions in force in the international business. The strengthening of foreign currencies in areas where we operate outside of the U.S. dollar unfavorably impacted SG&A by \$1 million, or 25% of the total increase.

Table Of Contents

Operating Income. Operating income was \$41 million for the three months ended June 30, 2018, as compared to \$17 million for the three months ended June 30, 2017, an improvement of \$24 million.

U.S. Segment—Operating income for our U.S. segment was \$37 million for the three months ended June 30, 2018 compared to \$21 million for the three months ended June 30, 2017. The \$16 million increase in operating income was driven by higher sales.

Canada Segment—Operating income for our Canada segment was \$2 million for the three months ended June 30, 2018 as compared to \$1 million for the three months ended June 30, 2017.

International Segment—Operating income for our international segment was \$2 million for the three months ended June 30, 2018 as compared to an operating loss of \$5 million for the three months ended June 30, 2017. The \$7 million improvement in operating income was primarily attributable to cost reduction actions taken in the second half of 2017.

Interest Expense. Our interest expense was \$10 million and \$8 million for the three month periods ended June 30, 2018 and 2017, respectively. The increase in interest expense was primarily attributable to higher average debt levels during the second quarter of 2018 as compared to the second quarter of 2017 as we invested in additional inventory to support expected growth.

Other (Expense) Income. Our other expense was \$1 million for the three month period ended June 30, 2018 as compared to \$0 million for the three month period ending June 30, 2017. Other expense for the three months ended June 30, 2018 included a \$1 million charge for the write off of debt issuance costs associated with the repricing of our Term Loan.

Income Tax Expense. Our income tax expense was \$8 million for the three months ended June 30, 2018 as compared to \$3 million for the three months ended June 30, 2017. For interim periods, our income tax expense is computed based upon our estimated annual effective tax rate and any discrete items that impact the interim periods. Our effective tax rates were 27% and 33% for the three months ended June 30, 2018 and 2017, respectively. Our rates generally differ from the U.S. federal statutory rates of 21% and 35% for the three months ended June 30, 2018 and 2017, respectively, as a result of state income taxes and differing foreign income tax rates. The 2018 effective tax rate exceeds the U.S. statutory rate primarily as a result of pre-tax losses in certain foreign jurisdictions with no corresponding tax benefit.

Net Income. Our net income was \$22 million for the three months ended June 30, 2018 as compared to \$6 million for the three months ended June 30, 2017, an improvement of \$16 million.

Adjusted EBITDA. Adjusted EBITDA, a non-GAAP financial measure, was \$78 million (7.2% of sales) for the three months ended June 30, 2018 as compared to \$44 million (4.8% of sales) for the three months ended June 30, 2017.

We define Adjusted EBITDA as net income plus interest, income taxes, depreciation and amortization, amortization of intangibles and certain other expenses, including non-cash expenses, (such as equity-based compensation, severance and restructuring, changes in the fair value of derivative instruments and asset impairments, including inventory) and plus or minus the impact of our LIFO inventory costing methodology.

We believe Adjusted EBITDA provides investors a helpful measure for comparing our operating performance with the performance of other companies that may have different financing and capital structures or tax rates. We believe it is a useful indicator of our operating performance without regard to items, such as amortization of intangibles, which can vary substantially from company to company depending upon the nature and extent of acquisitions. Similarly, the impact of the LIFO inventory costing method can cause results to vary substantially from company to company depending upon whether they elect to utilize LIFO and depending upon which method they may elect. We use Adjusted EBITDA as a key performance indicator in managing our business. We believe that net income is the financial measure calculated and presented in accordance with U.S. generally accepted accounting principles that is most directly comparable to Adjusted EBITDA.

Table Of Contents

The following table reconciles Adjusted EBITDA, a non-GAAP financial measure, with net income, as derived from our financial statements (in millions):

| | Three Months Ended | |
|--|--------------------------|---------------------|
| | June 30, 2018 | June 30, 2017 |
| Net income | \$ 22 | \$ 6 |
| Income tax expense | 8 | 3 |
| Interest expense | 10 | 8 |
| Depreciation and amortization | 6 | 6 |
| Amortization of intangibles | 11 | 11 |
| Increase in LIFO reserve | 15 | 5 |
| Change in fair value of derivative instruments | 1 | (1) |
| Equity-based compensation expense | 3 | 5 |
| Write off of debt issuance costs | 1 | - |
| Litigation settlement | - | 3 |
| Foreign currency losses (gains) | 1 | (2) |
| Adjusted EBITDA | \$ 78 | \$ 44 |

Six Months Ended June 30, 2018 Compared to the Six Months Ended June 30, 2017

The breakdown of our sales by sector for the six months ended June 30, 2018 and 2017 was as follows (in millions):

| | Six Months Ended | | | |
|------------|------------------|------|---------------|------|
| | June 30, 2018 | | June 30, 2017 | |
| Upstream | \$ 609 | 29% | \$ 503 | 28% |
| Midstream | 882 | 42% | 791 | 44% |
| Downstream | 601 | 29% | 490 | 28% |
| | \$ 2,092 | 100% | \$ 1,784 | 100% |

Table Of Contents

For the six months ended June 30, 2018 and 2017, the following table summarizes our results of operations (in millions):

| | Six Months Ended | | \$ Change | % Change |
|--|------------------|---------------|-----------|----------|
| | June 30, 2018 | June 30, 2017 | | |
| Sales: | | | | |
| U.S. | \$ 1,684 | \$ 1,386 | \$ 298 | 22% |
| Canada | 158 | 146 | 12 | 8% |
| International | 250 | 252 | (2) | (1%) |
| Consolidated | \$ 2,092 | \$ 1,784 | \$ 308 | 17% |
| Operating income (loss): | | | | |
| U.S. | \$ 65 | \$ 32 | \$ 33 | N/M |
| Canada | 4 | 4 | - | N/M |
| International | 3 | (5) | 8 | N/M |
| Consolidated | 72 | 31 | 41 | N/M |
| Interest expense | (18) | (15) | (3) | 20% |
| Other income | 1 | - | 1 | N/M |
| Income tax expense | (15) | (4) | (11) | N/M |
| Net income | 40 | 12 | 28 | N/M |
| Series A preferred stock dividends | 12 | 12 | - | N/M |
| Net income attributable to common stockholders | \$ 28 | \$ - | \$ 28 | N/M |
| Gross profit | \$ 346 | \$ 289 | \$ 57 | 20% |
| Adjusted Gross Profit (1) | \$ 402 | \$ 328 | \$ 74 | 23% |
| Adjusted EBITDA (1) | \$ 137 | \$ 80 | \$ 57 | 71% |

(1) Adjusted Gross Profit and Adjusted EBITDA are non-GAAP financial measures. For a reconciliation of these measures to an equivalent GAAP measure, see pages 23-24 herein.

Sales. Our sales were \$2,092 million for the six months ended June 30, 2018 as compared to \$1,784 million for the six months ended June 30, 2017, an increase of \$308 million, or 17%. The strengthening of foreign currencies in areas where we operate outside of the U.S. dollar favorably impacted sales by \$23 million, or 1%.

U.S. Segment—Our U.S. sales increased to \$1,684 million for the six months ended June 30, 2018 from \$1,386 million for the six months ended June 30, 2017. This \$298 million, or 22%, increase reflected a \$68 million increase in the upstream sector, a \$122 million increase in the midstream sector and a \$108 million increase in the downstream sector. The increase in the midstream sector is related to increased activity in the gas utility and transmission and gathering subsectors with several of our customers, and the increase in the upstream sector is related to the increase in rig count and well completions. The increase in the downstream sector is primarily related to increased project work, turnaround activity and growth from new contracts.

Canada Segment—Our Canada sales increased to \$158 million for the six months ended June 30, 2018 from \$146 million for the six months ended June 30, 2017, an increase of \$12 million, or 8%. Canadian sales were favorably impacted by \$6 million, or 4%, as a result of the stronger Canadian dollar relative to the U.S. dollar.

International Segment—Our International sales decreased to \$250 million for the six months ended June 30, 2018 from \$252 million for the same period in 2017. The \$2 million, or 1%, decrease included the offsetting impacts of a \$28 million increase in the upstream business related to project activity in Kazakhstan and a \$28 million decline in the midstream sector related primarily to an Australian line pipe project from 2017 with no such project work in the first half of 2018. The strengthening of foreign currencies in areas where we operate outside of the U.S. dollar favorably impacted sales by \$17 million, or 7%.

Gross Profit. Our gross profit was \$346 million (16.5% of sales) for the six months ended June 30, 2018 as compared to \$289 million (16.2% of sales) for the six months ended June 30, 2017. The \$57 million increase was primarily attributable to

Table Of Contents

the increase in sales volumes. Our LIFO inventory costing methodology resulted in an increase in cost of sales, as compared to average cost, of \$22 million and \$6 million in the first half of 2018 and 2017, respectively. Excluding the impact of LIFO, gross profit percentage improved by 110 basis points. While the first half of 2018 included a higher level of major project sales as compared to the first half of 2017, we benefited from a lower mix of lower margin line pipe sales. This combined with a favorable inflationary pricing environment drove the 110 basis point improvement in gross margins.

Adjusted Gross Profit. Adjusted Gross Profit increased to \$402 million (19.2% of sales) for the six months ended June 30, 2018 from \$328 million (18.4% of sales) for the six months ended June 30, 2017, an increase of \$74 million. Adjusted Gross Profit is a non-GAAP financial measure. We define Adjusted Gross Profit as sales, less cost of sales, plus depreciation and amortization, plus amortization of intangibles, and plus or minus the impact of our LIFO inventory costing methodology. We present Adjusted Gross Profit because we believe it is a useful indicator of our operating performance without regard to items, such as amortization of intangibles, that can vary substantially from company to company depending upon the nature and extent of acquisitions. Similarly, the impact of the LIFO inventory costing method can cause results to vary substantially from company to company depending upon whether they elect to utilize LIFO and depending upon which method they may elect. We use Adjusted Gross Profit as a key performance indicator in managing our business. We believe that gross profit is the financial measure calculated and presented in accordance with U.S. generally accepted accounting principles that is most directly comparable to Adjusted Gross Profit.

The following table reconciles Adjusted Gross Profit, a non-GAAP financial measure, with gross profit, as derived from our financial statements (in millions):

| | Six Months Ended | | Six Months Ended | |
|-------------------------------|---------------------|---------------------------|---------------------|---------------------------|
| | June 30, 2018 | Percentage of Revenue* | June 30, 2017 | Percentage of Revenue* |
| Gross profit, as reported | \$ 346 | 16.5% | \$ 289 | 16.2% |
| Depreciation and amortization | 12 | 0.6% | 11 | 0.6% |
| Amortization of intangibles | 22 | 1.1% | 22 | 1.2% |
| Increase in LIFO reserve | 22 | 1.1% | 6 | 0.3% |
| Adjusted Gross Profit | \$ 402 | 19.2% | \$ 328 | 18.4% |

*Does not foot due to rounding.

Selling, General and Administrative (“SG&A”) Expenses. Our SG&A expenses were \$274 million for the six months ended June 30, 2018 as compared to \$258 million for the six months ended June 30, 2017. The \$16 million increase in SG&A is primarily related to an increase in employee-related costs, including wage and incentive increases following three years of wage freezes and incentive reductions as a result of the downturn in our business. Further, we have also incurred incremental volume-related operating costs due to higher activity levels. The strengthening of foreign currencies in areas where we operate outside of the U.S. dollar unfavorably impacted SG&A by \$4 million, or 25% of the total increase.

Operating Income. Operating income was \$72 million for the six months ended June 30, 2018, as compared to \$31 million for the six months ended June 30, 2017, an improvement of \$41 million.

U.S. Segment—Operating income for our U.S. segment was \$65 million for the six months ended June 30, 2018 compared to \$32 million for the six months ended June 30, 2017. The \$33 million increase in operating income was driven by higher sales partially offset by the increase in SG&A.

Canada Segment—Operating income for our Canada segment was \$4 million for the six months ended June 30, 2018 and 2017.

International Segment—Operating income for our international segment was \$3 million for the six months ended June 30, 2018 as compared to a \$5 million operating loss for the six months ended June 30, 2017. The \$8 million improvement in operating income was primarily attributable to cost reduction actions taken in the second half of 2017.

Interest Expense. Our interest expense was \$18 million and \$15 million for the six month periods ended June 30, 2018 and June 30, 2017. The increase in interest expense was primarily attributable to higher average debt levels during the first six months of 2018 as compared to the first six months of 2017 as we invested in additional inventory to support expected growth.

Other Income. Our other income was \$1 million for the six month period ended June 30, 2018 as compared to \$0 million for the six month period ending June 30, 2017. Other income for the six months ended June 30, 2018 included \$1 million of income related to the change in fair value of derivatives and a \$1 million charge for the write off of debt issuance costs

Table Of Contents

associated with the refinancing amendment of our Term Loan. Other expense for the six months ended June 30, 2017 included a \$3 million charge associated with the settlement of a litigation matter and a \$2 million foreign currency gain.

Income Tax Expense. Our income tax expense was \$15 million for the six months ended June 30, 2018 as compared to \$4 million for the six months ended June 30, 2017. For interim periods, our income tax expense is computed based upon our estimated annual effective tax rate and any discrete items that impact the interim periods. Our effective tax rates were 27% and 25% for the six months ended June 30, 2018 and 2017, respectively. Our rates generally differ from the U.S. federal statutory rates of 21% and 35% for the six months ended June 30, 2018 and 2017, respectively, as a result of state income taxes and differing foreign income tax rates. The 2018 effective tax rate exceeds the U.S. statutory rate primarily as a result of pre-tax losses in certain foreign jurisdictions with no corresponding tax benefit. The 2017 effective tax rate was below the U.S. statutory rate as a result of a benefit related to foreign currency exchange losses and the adoption of ASU 2016-09, Compensation – Stock Compensation, which resulted in a discrete tax benefit of \$2 million related to the vesting of stock awards.

Net Income. Our net income was \$40 million for the six months ended June 30, 2018 as compared to \$12 million for the six months ended June 30, 2017, an improvement of \$28 million.

Adjusted EBITDA. Adjusted EBITDA, a non-GAAP financial measure, was \$137 million (6.5% of sales) for the six months ended June 30, 2018 as compared to \$80 million (4.5% of sales) for the six months ended June 30, 2017.

We define Adjusted EBITDA as net income plus interest, income taxes, depreciation and amortization, amortization of intangibles and certain other expenses, including non-cash expenses, (such as equity-based compensation, severance and restructuring, changes in the fair value of derivative instruments and asset impairments, including inventory) and plus or minus the impact of our LIFO inventory costing methodology.

We believe Adjusted EBITDA provides investors a helpful measure for comparing our operating performance with the performance of other companies that may have different financing and capital structures or tax rates. We believe it is a useful indicator of our operating performance without regard to items, such as amortization of intangibles, which can vary substantially from company to company depending upon the nature and extent of acquisitions. Similarly, the impact of the LIFO inventory costing method can cause results to vary substantially from company to company depending upon whether they elect to utilize LIFO and depending upon which method they may elect. We use Adjusted EBITDA as a key performance indicator in managing our business. We believe that net income is the financial measure calculated and presented in accordance with U.S. generally accepted accounting principles that is most directly comparable to Adjusted EBITDA.

The following table reconciles Adjusted EBITDA, a non-GAAP financial measure, with net income, as derived from our financial statements (in millions):

| | Six Months | |
|--|------------|-------|
| | Ended | |
| | June | June |
| | 30, | 30, |
| | 2018 | 2017 |
| Net income | \$ 40 | \$ 12 |
| Income tax expense | 15 | 4 |
| Interest expense | 18 | 15 |
| Depreciation and amortization | 12 | 11 |
| Amortization of intangibles | 22 | 22 |
| Increase in LIFO reserve | 22 | 6 |
| Change in fair value of derivative instruments | (1) | - |
| Equity-based compensation expense | 7 | 9 |
| Write off of debt issuance costs | 1 | - |
| Litigation settlement | - | 3 |
| Foreign currency losses (gains) | 1 | (2) |
| Adjusted EBITDA | \$ 137 | \$ 80 |

Table Of Contents

Liquidity and Capital Resources

Our primary sources of liquidity consist of cash generated from our operating activities, existing cash balances and availability under our Global ABL Facility. At June 30, 2018, our total liquidity, including cash on hand, was \$445 million. Our ability to generate sufficient cash flows from our operating activities will continue to be primarily dependent on our sales of products and services to our customers at margins sufficient to cover our fixed and variable expenses. As of June 30, 2018 and December 31, 2017, we had cash of \$31 million and \$48 million, respectively, all of which was maintained in the accounts of our various foreign subsidiaries and, if those amounts were transferred among countries or repatriated to the U.S., those amounts may be subject to additional tax liabilities, which would be recognized in our financial statements in the period during which the transfer decision was made. We currently have the intent and ability to indefinitely reinvest the cash held by our non-Canadian foreign subsidiaries and, pending further analysis of the impact of the Tax Act, there are currently no plans for the repatriation of those amounts. During the first quarter of 2018, we repatriated \$30 million from our Canadian subsidiaries.

Our primary credit facilities consist of a seven-year Term Loan maturing in September 2024 with an original principal amount of \$400 million and a five-year \$800 million Global ABL Facility that provides \$675 million in revolver commitments in the United States, \$65 million in Canada, \$18 million in Norway, \$15 million in Australia, \$13 million in the Netherlands, \$7 million in the United Kingdom and \$7 million in Belgium. As of June 30, 2018, the outstanding balance on our Term Loan, net of original issue discount and issuance costs, was \$395 million. The Global ABL Facility matures in September 2022. The Global ABL Facility contains an accordion feature that allows us to increase the principal amount of the facility by up to \$200 million, subject to securing additional lender commitments. As of June 30, 2018, we had \$313 million of borrowings outstanding and \$414 million of Excess Availability, as defined under our Global ABL Facility. Availability is dependent on a borrowing base comprised of a percentage of eligible accounts receivable and inventory which is subject to redetermination from time to time.

Our credit ratings are below “investment grade” and as such could impact both our ability to raise new funds as well as the interest rates on our future borrowings. Our ability to incur additional debt is restricted by our existing obligations. We were in compliance with the covenants contained in our various credit facilities as of and during the six months ended June 30, 2018. We do not believe the 2019 implementation of the new lease accounting standard will impact our compliance with debt covenants, as our credit facilities contain provisions that grandfather our current method of accounting for leases for debt compliance purposes.

We believe our sources of liquidity will be sufficient to satisfy the anticipated cash requirements associated with our existing operations for at least the next twelve months. However, our future cash requirements could be higher than we currently expect as a result of various factors. Additionally, our ability to generate sufficient cash from our operating activities depends on our future performance, which is subject to general economic, political, financial, competitive and other factors beyond our control. We may, from time to time, seek to raise additional debt or equity financing or re-price or refinance existing debt in the public or private markets, based on market conditions. Any such capital markets activities would be subject to market conditions, reaching final agreement with lenders or investors, and other factors, and there can be no assurance that we would successfully consummate any such transactions.

In November 2015, the Company's board of directors authorized a share repurchase program for common stock up to \$100 million, which was increased in November 2016 to \$125 million. In the first quarter of 2017, the company completed the repurchase of all shares authorized under the program. Under this program, we purchased 8,537,410 shares at a total cost of \$125 million.

In October 2017, the Company's board of directors authorized a new share repurchase program for common stock of up to \$100 million. During the first half of 2018, we completed the repurchases of all shares authorized under the program by purchasing 2,871,204 shares at a total cost of \$50 million. Under this program, we purchased 6,085,520 shares at a cost of \$100 million.

In total, under both programs, we have purchased a combined 14,622,930 shares at a total cost of \$225 million.

Table Of Contents

Cash Flows

The following table sets forth our cash flows for the periods indicated below (in millions):

| | Six Months Ended | |
|---|---------------------|---------------------|
| | June 30, 2018 | June 30, 2017 |
| Net cash (used in) provided by: | | |
| Operating activities | \$ (139) | \$ (24) |
| Investing activities | (9) | (14) |
| Financing activities | 134 | (37) |
| Net decrease in cash and cash equivalents | \$ (14) | \$ (75) |

Operating Activities

Net cash used in operating activities was \$139 million during the six months ended June 30, 2018 compared to \$24 million during the six months ended June 30, 2017. The increase in cash used in operations was primarily the result of working capital expansion in response to the increase in sales activity. Working capital growth used cash of \$240 million in the first six months of 2018 compared to \$81 million in the first six months of 2017. In particular, growth in accounts receivable utilized \$157 million of cash in the first six months of 2018 as a result of the 17% increase in sales relative to the first six months 2017 when accounts receivable utilized cash of \$117 million. Growth in inventory required to support higher sales levels utilized \$201 million of cash in the first six months of 2018 as compared to \$33 million in the same period of 2017. These uses of cash were offset by \$116 million generated from an increase in accounts payable in 2018 as compared to \$68 million in 2017, which was attributable to higher purchasing activities.

Investing Activities

Net cash used in investing activities was \$9 million for the six months ended June 30, 2018, compared to \$14 million for the six months ended June 30, 2017 which represented our capital expenditures for both periods.

Financing Activities

Net cash provided by financing activities was \$134 million for the six months ended June 30, 2018 compared to a net cash use of \$37 million for the six months ended June 30, 2017. In the first six months of 2018 and 2017, we had net borrowings of \$184 million and \$0 million and used \$50 million and \$18 million to fund purchases of our common stock, respectively. We used \$12 million to pay dividends on preferred stock for the six months ended June 30, 2018 and 2017.

Critical Accounting Policies

The preparation of financial statements, in conformity with accounting principles generally accepted in the United States of America, requires management to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expense in the financial statements. Management bases its estimates on

historical experience and other assumptions, which it believes are reasonable. If actual amounts are ultimately different from these estimates, the revisions are included in our results of operations for the period in which the actual amounts become known.

Accounting policies are considered critical when they require management to make assumptions about matters that are highly uncertain at the time the estimates are made and when there are different estimates that management reasonably could have made, which would have a material impact on the presentation of our financial condition, changes in our financial condition or results of operations. For a description of our critical accounting policies, see “Item 7: “Management’s Discussion and Analysis of Financial Condition and Results from Operations” in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are primarily exposed to the market risk associated with unfavorable movements in interest rates, foreign currencies and steel price volatility. In the first quarter of 2018, we entered into a \$250 million interest rate swap to fix a portion of our variable interest rate exposure. Other than the interest rate swap, there have been no material changes to our market risk policies or our market risk sensitive instruments and positions as described in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017.

Table Of Contents

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of disclosure controls and procedures.

As of June 30, 2018, we have reviewed, under the direction of our Chief Executive Officer and Chief Financial Officer, the Company's disclosure controls and procedures, as defined in Exchange Act Rule 13a-15(e). Based upon and as of the date of that review, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective to ensure that information required to be disclosed in the reports that the Company files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Company's management, including the Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosures.

As part of a continuing effort to improve the Company's business processes, management is evaluating its internal controls and may update certain controls to accommodate any modifications to its business processes or accounting procedures.

Changes in internal control over financial reporting.

There were no changes in our internal control over financial reporting that occurred during the second quarter of 2018 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Table Of Contents

Part II—other information

ITEM 1. LEGAL PROCEEDINGS

From time to time, we have been subject to various claims and involved in legal proceedings incidental to the nature of our businesses. We maintain insurance coverage to reduce financial risk associated with certain of these claims and proceedings. It is not possible to predict the outcome of these claims and proceedings. However, in our opinion, there are no pending legal proceedings that are likely to have a material effect on our business, financial condition, results of operations or cash flows, although it is possible that the resolution of certain actual, threatened or anticipated claims or proceedings could have a material adverse effect on our results of operations in the period of resolution.

Also, from time to time, in the ordinary course of our business, our customers may claim that the products that we distribute are either defective or require repair or replacement under warranties that either we or the manufacturer may provide to the customer. These proceedings are, in the opinion of management, ordinary and routine matters incidental to our normal business. Our purchase orders with our suppliers generally require the manufacturer to indemnify us against any product liability claims, leaving the manufacturer ultimately responsible for these claims. In many cases, state, provincial or foreign law provides protection to distributors for these sorts of claims, shifting the responsibility to the manufacturer. In some cases, we could be required to repair or replace the products for the benefit of our customer and seek recovery from the manufacturer for our expense. In the opinion of management, the ultimate disposition of these claims and proceedings is not expected to have a material adverse effect on our financial condition, results of operations or cash flows.

For information regarding asbestos cases in which we are a defendant and other claims and proceedings, see Note 10 - Commitments and Contingencies to our unaudited condensed consolidated financial statements.

Item 1A. Risk Factors

We are affected by risks specific to us as well as factors that affect all businesses operating in a global market. The significant factors known to us that could materially adversely affect our business, financial condition or operating results are described in Part I, Item 2 of this Quarterly Report on Form 10-Q and in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2017 under “Risk Factors”.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

A summary of our purchases of MRC Global Inc. common stock during the second quarter of fiscal year 2018 is as follows:

| Total Number of Shares Purchased (1) | Average Price Paid per Share | Total number of Shares Purchased as Part of Publicly Announced Plans | Maximum Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs |
|--------------------------------------|------------------------------|--|--|
|--------------------------------------|------------------------------|--|--|

| | | | or Programs | | |
|---------|-----------|----|-------------|-----------|------|
| Apr 1 - | | | | | |
| Apr 30 | 1,149,607 | \$ | 17.40 | 1,144,379 | \$ - |
| May 1 - | | | | | |
| May 31 | 14,040 | \$ | 19.13 | - | \$ - |
| Jun 1 - | | | | | |
| Jun 30 | 14 | \$ | 20.02 | - | \$ - |
| | 1,153,661 | | | | |

(1) We purchased 9,282 shares in connection with funding employee income tax withholding obligations arising upon the lapse of restrictions on restricted shares.

Item 3. Defaults Upon Senior Securities

None.

28

Table Of Contents

Item 4. MINING SAFETY DISCLOSURES

None.

Item 5. Other Information

None.

29

Table Of Contents

Item 6. Exhibits

| Number | Description |
|--------|---|
| 31.1* | <u>Certification of the Chief Executive Officer pursuant to Rules 13a-14(a) and 15d-14(a) promulgated under the Securities Exchange Act of 1934, as amended, and Item 601(b)(31) of Regulation S-K, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u> |
| 31.2* | <u>Certification of the Chief Financial Officer pursuant to Rules 13a-14(a) and 15d-14(a) promulgated under the Securities Exchange Act of 1934, as amended, and Item 601(b)(31) of Regulation S-K, as adopted pursuant to Section 302 of the</u> |

Sarbanes-Oxley
Act of 2002.

32** Certification of
the Chief
Executive
Officer and the
Chief Financial
Officer pursuant
to 18 U.S.C.
Section 1350, as
adopted
pursuant to
Section 906 of
the
Sarbanes-Oxley
Act of 2002.

100* The following
financial
information
from MRC
Global Inc.'s
Quarterly Report
on Form 10-Q
for the period
ended June 30,
2018, formatted
in Extensible
Business
Reporting
Language
(XBRL): (i) the
Condensed
Consolidated
Balance Sheets
at June 30,
2018 and
December 31,
2017, (ii) the
Condensed
Consolidated
Statements of
Operations for
the three and six
month periods
ended June 30,
2018 and 2017,
(iii) the
Condensed
Consolidated

Statements of
Comprehensive
Income for the
three and six
month periods
ended June 30,
2018 and 2017,
(iv) the
Condensed
Consolidated
Statements of
Cash Flows for
the six month
periods ended
June 30, 2018
and 2017 and
(v) Notes to
Condensed
Consolidated
Financial
Statements.

101* Interactive data
file.

* Filed herewith.

** Furnished herewith.

Table Of Contents

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: August 2, 2018

MRC GLOBAL INC.

By: /s/ James E. Braun

James E. Braun

Executive Vice President and Chief Financial Officer