MASCO CORP /DE/
Form 10-Q
October 31, 2007

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

FORM 10-Q

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

For the quarterly period ended September 30, 2007

Commission file number: 1-5794

Masco Corporation

(Exact name of Registrant as Specified in Charter)

Delaware	**38-1794485**
(State or Other Jurisdiction of Incorporation)	(IRS Employer Identification No.)
21001 Van Born Road, Taylor, Michigan	**48180**
(Address of Principal Executive Offices)	(Zip Code)

(313) 274-7400

(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.

þ Yes o No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated þ Accelerated o Non-accelerated o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

o Yes þ No

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

Class	Shares Outstanding at October 30, 2007
Common stock, par value $1.00 per share	368,800,000

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Computation of Ratio of Earnings
Certification by Chief Executive Officer Required by Rule 13a-14(a) or 15d-14(a)
Certification by Chief Financial Officer Required by Rule 13a-14(a) or 15d-14(a)
Certification Required by Rule 13a-14(b) or 15(d)-14(b)

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MASCO CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)
September 30, 2007 and December 31, 2006
(In Millions Except Share Data)

	September 30, 2007	December 31, 2006
ASSETS		
Current assets:		
Cash and cash investments	$ 690	$ 1,958
Accounts and notes receivable, net	1,762	1,613
Prepaid expenses and other	320	281
Inventories:		
Finished goods	600	610
Raw material	450	480
Work in process	157	173
	1,207	1,263
Total current assets	3,979	5,115
Property and equipment, net	2,351	2,363
Goodwill	4,108	3,957
Other intangible assets, net	371	306
Other assets	523	584
Total assets	$ 11,332	$ 12,325
LIABILITIES		
Current liabilities:		
Notes payable	$ 24	$ 1,446
Accounts payable	839	815
Accrued liabilities	1,149	1,128
Total current liabilities	2,012	3,389
Long-term debt	4,043	3,533
Deferred income taxes and other	1,074	932
Total liabilities	7,129	7,854
Commitments and contingencies		
SHAREHOLDERS EQUITY		
Common shares, par value $1 per share	361	384

Authorized shares: 1,400,000,000; Issued and outstanding: 2007 - 361,260,000; 2006 - 383,890,000				
Retained earnings		3,216		3,575
Accumulated other comprehensive income		626		512
Total shareholders equity		4,203		4,471
Total liabilities and shareholders equity	$	11,332	$	12,325

See notes to condensed consolidated financial statements.

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MASCO CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (Unaudited)
For the Three Months and Nine Months Ended September 30, 2007 and 2006
(In Millions Except Per Common Share Data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	**2006**	**2007**	**2006**
Net sales	$ 3,059	$ 3,279	$ 9,072	$ 9,787
Cost of sales	2,197	2,360	6,551	7,021
Gross profit	862	919	2,521	2,766
Selling, general and administrative expenses	488	520	1,525	1,561
Impairment charge for goodwill				10
Operating profit	374	399	996	1,195
Other income (expense), net:				
Impairment charge for investments	(12)	(8)	(22)	(86)
Interest expense	(65)	(54)	(197)	(171)
Other, net	32	18	89	84
	(45)	(44)	(130)	(173)
Income from continuing operations before income taxes, minority interest and cumulative effect of accounting change, net	329	355	866	1,022
Income taxes	109	123	302	354
Income from continuing operations before minority interest and cumulative effect of accounting change, net	220	232	564	668
Minority interest	11	7	27	21
Income from continuing operations before cumulative effect of accounting change, net	209	225	537	647
(Loss) income from discontinued operations, net	(4)	27		31
Cumulative effect of accounting change, net				(3)
Net income	$ 205	$ 252	$ 537	$ 675

Earnings per common share:
Basic:

Income from continuing operations before cumulative effect of accounting change, net	$ .57	$ .58	$ 1.44	$ 1.63
(Loss) income from discontinued operations, net	(.01)	.07		.08
Cumulative effect of accounting change, net				(.01)
Net income	$ .56	$ .65	$ 1.44	$ 1.70
Diluted:				
Income from continuing operations before cumulative effect of accounting change, net	$ .57	$ .57	$ 1.43	$ 1.61
(Loss) income from discontinued operations, net	(.01)	.07		.08
Cumulative effect of accounting change, net				(.01)
Net income	$ .56	$ .64	$ 1.43	$ 1.68
Cash dividends per common share:				
Declared	$ .23	$ .22	$ .69	$ .66
Paid	$ .23	$ .22	$ .68	$ .64

See notes to condensed consolidated financial statements.

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MASCO CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)
For the Nine Months Ended September 30, 2007 and 2006
(In Millions)

	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
CASH FLOWS FROM (FOR) OPERATING ACTIVITIES:		
Cash provided by operations	$ 850	$ 1,048
(Increase) in receivables	(137)	(191)
Decrease (increase) in inventories	67	(178)
Increase in accounts payable and accrued liabilities, net	35	94
Net cash from operating activities	815	773
CASH FLOWS FROM (FOR) FINANCING ACTIVITIES:		
Increase in debt	2	43
Payment of debt	(34)	(22)
Retirement of notes	(1,425)	(827)
Issuance of notes, net of issuance costs	596	
Purchase of Company common stock	(804)	(789)
Issuance of Company common stock	60	25
Cash dividends paid	(262)	(262)
Net cash (for) financing activities	(1,867)	(1,832)
CASH FLOWS FROM (FOR) INVESTING ACTIVITIES:		
Capital expenditures	(174)	(282)
Purchases of auction rate securities	(1,047)	(503)
Proceeds from disposition of auction rate securities	1,025	569
Purchases of marketable securities		(141)
Proceeds from disposition of:		
Marketable securities	53	151
Other financial investments, net	63	36
Businesses, net of cash disposed	11	145
Property and equipment	41	4
Acquisition of companies, net of cash acquired	(190)	(15)
Other, net	(25)	(42)
Net cash (for) investing activities	(243)	(78)
Effect of exchange rate changes on cash and cash investments	31	11

CASH AND CASH INVESTMENTS:		
(Decrease) for the period	(1,264)	(1,126)
At January 1	1,958	1,870
Cash at businesses held for sale	(4)	
At September 30	$ 690	$ 744

See notes to condensed consolidated financial statements.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

A. In the opinion of the Company, the accompanying unaudited condensed consolidated financial statements contain all adjustments, of a normal recurring nature, necessary to present fairly its financial position at September 30, 2007 and the results of operations for the three months and nine months ended September 30, 2007 and 2006 and changes in cash flows for the nine months ended September 30, 2007 and 2006. The condensed consolidated balance sheet at December 31, 2006 was derived from audited financial statements.

Certain prior-year amounts have been reclassified to conform to the 2007 presentation in the condensed consolidated financial statements. The results of operations related to 2007 and 2006 discontinued operations have been separately stated in the accompanying condensed consolidated statements of income for the three months and nine months ended September 30, 2007 and 2006. In the Company s condensed consolidated statements of cash flows for the nine months ended September 30, 2007 and 2006, the cash flows of discontinued operations are not separately classified.

Recently Issued Accounting Pronouncements. In February 2007, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of SFAS No. 115, (SFAS No. 159). SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The adoption of SFAS No. 159 is optional and is effective January 1, 2008. The Company has elected not to adopt SFAS No. 159.

B. At September 30, 2007, outstanding stock-based incentives were in the form of long-term stock awards, stock options, phantom stock awards and stock appreciation rights. Additionally, the Company s 1997 Non-Employee Directors Stock Plan (the 1997 Plan) provides for the payment of part of the compensation to non-employee Directors in Company common stock. Pre-tax compensation expense (income) and the related income tax benefit for stock-based incentives were as follows, in millions:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
Long-term stock awards	$ 12	$ 12	$ 41	$ 43
Stock options	11	18	36	36
Phantom stock awards and stock appreciation rights	(5)	(1)	(7)	(2)
Total	$ 18	$ 29	$ 70	$ 77
Income tax benefit	$ 7	$ 11	$ 26	$ 29

Long-Term Stock Awards

Long-term stock awards are granted to key employees and non-employee Directors of the Company and do not cause net share dilution inasmuch as the Company continues the practice of repurchasing and retiring an equal number of shares on the open market.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)

Note B continued:

The Company s long-term stock award activity was as follows, shares in millions:

	Nine Months Ended September 30,	
	2007	**2006**
Unvested stock award shares, January 1	9	9
Weighted average grant date fair value	$27	$25
Stock award shares granted	2	2
Weighted average grant date fair value	$31	$29
Stock award shares vested	2	2
Weighted average grant date fair value	$25	$24
Stock award shares forfeited		
Weighted average grant date fair value	$28	$26
Unvested stock award shares, September 30	9	9
Weighted average grant date fair value	$28	$27

At September 30, 2007, there was $189 million of unrecognized compensation expense related to unvested stock awards; such awards had a weighted average remaining vesting period of seven years.

The total market value (at the vesting date) of stock award shares which vested during the nine months ended September 30, 2007 was $47 million.

Stock Options

The Company granted 4,656,500 of stock option shares, including restoration stock option shares, in the first nine months of 2007 with a grant date exercise price range of $26 to $34 per share. In the first nine months of 2007, 1,847,400 stock option shares were forfeited (including options that expired unexercised).

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MASCO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)

Note B continued:

The Company s stock option activity was as follows, shares in millions:

	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
Option shares outstanding, January 1	26	27
Weighted average exercise price	$ 26	$ 26
Option shares granted, including restoration options	5	4
Weighted average exercise price	$ 30	$ 27
Option shares exercised	3	3
Aggregate intrinsic value on date of exercise **(A)**	$ 26 million	$ 18 million
Weighted average exercise price	$ 23	$ 25
Option shares forfeited	2	1
Weighted average exercise price	$ 30	$ 30
Option shares outstanding, September 30	26	27
Weighted average exercise price	$ 27	$ 26
Weighted average remaining option term (in years)	7	6
Option shares vested and expected to vest, September 30	26	27
Weighted average exercise price	$ 27	$ 26
Aggregate intrinsic value **(A)**	$ 16 million	$ 67 million
Weighted average remaining option term (in years)	7	6
Option shares exercisable (vested), September 30	13	13
Weighted average exercise price	$ 26	$ 25
Aggregate intrinsic value **(A)**	$ 14 million	$ 51 million
Weighted average remaining option term (in years)	5	5

(A) Aggregate intrinsic value is calculated using the Company s stock price at each respective date, less the exercise price (grant date price) multiplied by the number of shares.

At September 30, 2007, there was $87 million of unrecognized compensation expense (using the Black-Scholes option pricing model at the grant date) related to unvested stock options; such options had a weighted average vesting period of three years.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)

Note B concluded:

The weighted average grant date fair value of option shares granted and the assumptions used to estimate those values using a Black-Scholes option pricing model were as follows:

	Nine Months Ended September 30,	
	2007	2006
Weighted average grant date fair value	$ 9.11	$ 8.31
Risk-free interest rate	4.79%	4.90%
Dividend yield	2.93%	3.11%
Volatility factor	31.85%	34.21%
Expected option life	7 years	7 years

C. During the first nine months of 2007, the Company acquired several relatively small installation service businesses (Installation and Other Services segment), as well as Erickson Construction Company and Guy Evans, Inc. (Installation and Other Services segment). Erickson Construction Company, headquartered in Arizona, provides pre-fabricated wall panels and millwork for residential builders in Arizona, California and Nevada. Guy Evans, Inc., headquartered in California, is an installer of millwork, doors, windows and bath hardware for residential builders in California and Nevada. These two acquisitions allow the Company to expand the products and services it offers to its customers, and had combined annual sales in 2006 of approximately $200 million. The results of these acquisitions are included in the consolidated financial statements from the respective dates of acquisition. The aggregate net purchase price for all of these acquisitions was $188 million and included cash of $183 million and assumed debt of $5 million.

D. During the second quarter of 2007, the Company determined that a European business unit in the Decorative Architectural Products segment was not core to the Company s long-term growth strategy, and, accordingly, embarked on a plan of disposition. In accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, the Company has accounted for this business unit, as well as a business unit which was sold in 2006, as discontinued operations.

Selected financial information for the discontinued operations during the period owned by the Company, and the net losses reflecting the anticipated sale of the 2007 discontinued operation, which offset gains related to the receipt of final purchase price payments related to discontinued operations in prior years, was as follows, in millions:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
Net sales	$ 19	$ 33	$ 54	$ 100
Income from discontinued operations	$	$ 3	$ 2	$ 8
(Loss) gain on disposal of discontinued operations, net	(4)	50	(1)	51
(Loss) income before income taxes	(4)	53	1	59
Income tax		(26)		