

COMPX INTERNATIONAL INC  
Form 10-Q  
November 05, 2014

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES

EXCHANGE ACT OF 1934

For the quarter ended September 30, 2014

Commission file number 1-13905

COMPX INTERNATIONAL INC.

(Exact name of Registrant as specified in its charter)

|   |  |
|---|--|
| Delaware<br>(State or other jurisdiction of<br>Incorporation or organization) | 57-0981653<br>(IRS Employer<br>Identification No.) |
|---|--|

5430 LBJ Freeway, Suite 1700,

|   |                          |
|---|--------------------------|
| Three Lincoln Centre, Dallas, Texas<br>(Address of principal executive offices) | 75240-2697<br>(Zip Code) |
|---|--------------------------|

Registrant's telephone number, including area code (972) 448-1400

Indicate by checkmark:

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 a shorter period that the Registrant was required to file such

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reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company (as defined in Rule 12b-2 of the Exchange Act). Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No .

Number of shares of common stock outstanding on October 30, 2014:

Class A: 2,404,107

Class B: 10,000,000

COMPX INTERNATIONAL INC.

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## COMPX INTERNATIONAL INC.

## CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands)

| ASSETS                        | December<br>31,<br>2013 | September<br>30,<br>2014<br>(unaudited) |
|-------------------------------|-------------------------|---|
| Current assets:               |                         |   |
| Cash and cash equivalents     | \$38,753                | \$ 41,862                               |
| Accounts receivable, net      | 8,534                   | 11,640                                  |
| Inventories, net              | 13,235                  | 15,082                                  |
| Deferred income taxes         | 2,493                   | 2,493                                   |
| Prepaid expenses and other    | 596                     | 560                                     |
| Total current assets          | 63,611                  | 71,637                                  |
| Other assets:                 |                         |   |
| Goodwill                      | 23,742                  | 23,742                                  |
| Other noncurrent              | 573                     | 602                                     |
| Total other assets            | 24,315                  | 24,344                                  |
| Property and equipment:       |                         |   |
| Land                          | 4,928                   | 4,928                                   |
| Buildings                     | 20,523                  | 20,906                                  |
| Equipment                     | 57,799                  | 61,406                                  |
| Construction in progress      | 2,588                   | 594                                     |
|                               | 85,838                  | 87,834                                  |
| Less accumulated depreciation | 52,086                  | 54,699                                  |
| Net property and equipment    | 33,752                  | 33,135                                  |
| Total assets                  | \$ 121,678              | \$ 129,116                              |

## COMPX INTERNATIONAL INC.

## CONDENSED CONSOLIDATED BALANCE SHEETS (CONTINUED)

(In thousands)

|  | December<br>31,<br>2013 | September<br>30,<br>2014<br>(unaudited) |
|--|-------------------------|---|
| LIABILITIES AND STOCKHOLDERS' EQUITY       |                         |   |
| Current liabilities:                       |                         |   |
| Accounts payable and accrued liabilities   | \$9,705                 | \$ 11,536                               |
| Income taxes payable to affiliates         | 339                     | 1,068                                   |
| Other                                      | 6                       | 25                                      |
| Total current liabilities                  | 10,050                  | 12,629                                  |
| Noncurrent liabilities:                    |                         |   |
| Deferred income taxes                      | 6,900                   | 6,617                                   |
| Stockholders' equity:                      |                         |   |
| Preferred stock                            | —                       | —                                       |
| Class A common stock                       | 24                      | 24                                      |
| Class B common stock                       | 100                     | 100                                     |
| Additional paid-in capital                 | 55,265                  | 55,342                                  |
| Retained earnings                          | 49,339                  | 54,404                                  |
| Total stockholders' equity                 | 104,728                 | 109,870                                 |
| Total liabilities and stockholders' equity | \$ 121,678              | \$ 129,116                              |

Commitments and contingencies (Note 1)

See accompanying Notes to Condensed Consolidated Financial Statements.

## COMPX INTERNATIONAL INC.

## CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(In thousands, except per share data)

|   | Three months<br>ended<br>September 30,<br>2013    2014<br>(unaudited) |          | Nine months<br>ended<br>September 30,<br>2013    2014<br>(unaudited) |          |
|---|---|----------|--|----------|
| Net sales   | \$24,209  | \$26,473 | \$69,701   | \$79,102 |
| Cost of goods sold                                    | 16,695  | 18,331   | 48,557   | 54,598   |
| Gross profit  | 7,514   | 8,142    | 21,144   | 24,504   |
| Selling, general and administrative expense           | 4,537   | 4,710    | 13,790   | 13,872   |
| Operating income                                      | 2,977   | 3,432    | 7,354  | 10,632   |
| Interest income                                       | 5   | 7        | 32   | 19       |
| Interest expense                                      | (11 )   | —        | (127 )   | —        |
| Income before taxes                                   | 2,971   | 3,439    | 7,259  | 10,651   |
| Provision for income taxes                            | 1,015   | 1,210    | 2,593  | 3,726    |
| Net income  | \$1,956   | \$2,229  | \$4,666  | \$6,925  |
| <br>  |   |          |  |          |
| Basic and diluted net income per common share         | \$0.16  | \$0.18   | \$0.38   | \$0.56   |
| <br>  |   |          |  |          |
| Cash dividends per share                              | \$0.050   | \$0.050  | \$0.225  | \$0.150  |
| <br>  |   |          |  |          |
| Basic and diluted weighted average shares outstanding | 12,397  | 12,404   | 12,394   | 12,400   |

See accompanying Notes to Condensed Consolidated Financial Statements.

## COMPX INTERNATIONAL INC.

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

|   | Nine months ended<br>September 30,<br>2013      2014<br>(unaudited) |          |
|---|---|----------|
| Cash flows from operating activities:               |   |          |
| Net income  | \$4,666   | \$6,925  |
| Depreciation and amortization                       | 2,464   | 2,643    |
| Deferred income taxes                               | 742   | (283 )   |
| Other, net  | 214   | 341      |
| Change in assets and liabilities:                   |   |          |
| Accounts receivable, net                            | (2,161 )  | (3,159 ) |
| Inventories, net                                    | (1,884 )  | (2,030 ) |
| Accounts payable and accrued liabilities            | (820 )  | 1,984    |
| Accounts with affiliates                            | (11,825 )   | 728      |
| Income taxes  | —   | 9        |
| Other, net  | 738   | 36       |
| Net cash provided by (used in) operating activities | (7,866 )  | 7,194    |
| Cash flows from investing activities:               |   |          |
| Capital expenditures                                | (2,550 )  | (2,168 ) |
| Cash collected on note receivable                   | 3,034   | —        |
| Proceeds from sale of assets held for sale          | 1,559   | —        |
| Other, net  | (94 )   | (57 )    |
| Net cash provided by (used in) investing activities | 1,949   | (2,225 ) |
| Cash flows from financing activities:               |   |          |
| Dividends paid                                      | (2,789 )  | (1,860 ) |
| Repayment of long-term debt                         | (18,480)  | —        |
| Net cash used in financing activities               | (21,269)  | (1,860 ) |
| Cash and cash equivalents - net change from:        |   |          |
| Operating, investing and financing activities       | (27,186)  | 3,109    |
| Balance at beginning of period                      | 63,777  | 38,753   |
| Balance at end of period                            | \$36,591  | \$41,862 |
| Supplemental disclosures - cash paid for:           |   |          |
| Interest  | \$222   | \$—      |
| Income taxes  | 13,675  | 3,271    |

See accompanying Notes to Condensed Consolidated Financial Statements.





COMPX INTERNATIONAL INC.

## CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

Nine months ended September 30, 2014

(In thousands)

(unaudited)

|                               | Common<br>stock<br>Class Class |       | Additional<br>paid-in<br>capital | Retained<br>earnings | Total<br>stockholders'<br>equity |
|-------------------------------|--------------------------------|-------|----------------------------------|----------------------|----------------------------------|
|                               | A                              | B     |                                  |                      |                                  |
| Balance at December 31, 2013  | \$24                           | \$100 | \$55,265                         | \$49,339             | \$104,728                        |
| Net income                    | —                              | —     | —                                | 6,925                | 6,925                            |
| Issuance of common stock      | —                              | —     | 77                               | —                    | 77                               |
| Cash dividends                | —                              | —     | —                                | (1,860)              | (1,860)                          |
| Balance at September 30, 2014 | \$24                           | \$100 | \$55,342                         | \$54,404             | \$109,870                        |

See accompanying Notes to Condensed Consolidated Financial Statements.

COMPX INTERNATIONAL INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2014

(unaudited)

Note 1 – Organization and basis of presentation:

Organization. We (NYSE MKT: CIX) are 87% owned by NL Industries, Inc. (NYSE: NL) at September 30, 2014. We manufacture and sell component products (security products and recreational marine components). At September 30, 2014, (i) Valhi, Inc. (NYSE: VHI) held approximately 83% of NL's outstanding common stock and (ii) a wholly-owned subsidiary of Contran Corporation ("Contran") held an aggregate of approximately 94% of Valhi's outstanding common stock. Substantially all of Contran's outstanding voting stock is held by family trusts established for the benefit of Lisa K. Simmons and Serena Simmons Connelly, daughters of Harold C. Simmons, and their children (for which Ms. Lisa Simmons and Ms. Connelly are co-trustees) or is held directly by Ms. Lisa Simmons and Ms. Connelly or persons or entities related to them, including their step-mother Annette C. Simmons, the widow of Mr. Simmons. Prior to his death in December 2013, Mr. Simmons served as sole trustee of the family trusts. Under a voting agreement entered into by all of the voting stockholders of Contran, effective in February 2014 and as amended, the size of the board of directors of Contran was fixed at five members, Ms. Lisa Simmons, Ms. Connelly and Ms. Annette Simmons (and in the event of their death, their heirs) each has the right to designate one of the five members of the Contran board and the remaining two members of the Contran board must consist of members of Contran management. Ms. Lisa Simmons, Ms. Connelly, and Ms. Annette Simmons each serve as members of the Contran board. The voting agreement expires in February 2017 (unless Ms. Lisa Simmons, Ms. Connelly and Ms. Annette Simmons otherwise unanimously agree), and the ability of Ms. Lisa Simmons, Ms. Connelly, and Ms. Annette Simmons to each designate one member of the Contran board is dependent upon each of their continued beneficial ownership of at least 5% of the combined voting stock of Contran. Consequently, Ms. Lisa Simmons, Ms. Connelly and Ms. Annette Simmons may be deemed to control Contran, Valhi, NL and us.

Basis of presentation. Consolidated in this Quarterly Report are the results of CompX International Inc. and its subsidiaries. The unaudited Condensed Consolidated Financial Statements contained in this Quarterly Report have been prepared on the same basis as the audited Consolidated Financial Statements included in our Annual Report on Form 10-K for the year ended December 31, 2013 that we filed with the Securities and Exchange Commission ("SEC") on March 5, 2014 (the "2013 Annual Report"). In our opinion, we have made all necessary adjustments (which include only normal recurring adjustments) in order to state fairly, in all material respects, our consolidated financial position, results of operations and cash flows as of the dates and for the periods presented. We have condensed the Consolidated Balance Sheet at December 31, 2013 contained in this Quarterly Report as compared to our audited Consolidated Financial Statements at that date, and we have omitted certain information and footnote disclosures (including those related to the Consolidated Balance Sheet at December 31, 2013) normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"). Our results of operations for the interim periods ended September 30, 2014 may not be indicative of our operating results for the full year. The Condensed Consolidated Financial Statements contained in this Quarterly Report should be read in conjunction with our 2013 Consolidated Financial Statements contained in our 2013 Annual Report.

Unless otherwise indicated, references in this report to “we”, “us” or “our” refer to CompX International Inc. and its subsidiaries, taken as a whole.

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## Note 2 – Business segment information:

|                              | Three months<br>ended<br>September 30,<br>2013 |          | 2014           |          | Nine months<br>ended<br>September 30,<br>2013 |  | 2014           |  |
|------------------------------|--|----------|----------------|----------|---|--|----------------|--|
|                              | (In thousands)                                 |          | (In thousands) |          | (In thousands)                                |  | (In thousands) |  |
| Net sales:                   |  |          |                |          |   |  |                |  |
| Security Products            | \$21,457                                       | \$23,237 | \$61,258       | \$69,246 |   |  |                |  |
| Marine Components            | 2,752  | 3,236    | 8,443          | 9,856    |   |  |                |  |
| Total net sales              | \$24,209                                       | \$26,473 | \$69,701       | \$79,102 |   |  |                |  |
| Operating income:            |  |          |                |          |   |  |                |  |
| Security Products            | \$4,578  | \$4,694  | \$12,245       | \$14,235 |   |  |                |  |
| Marine Components            | (17 )  | 223      | 185            | 729      |   |  |                |  |
| Corporate operating expenses | (1,584 )                                       | (1,485 ) | (5,076 )       | (4,332 ) |   |  |                |  |
| Total operating income       | 2,977  | 3,432    | 7,354          | 10,632   |   |  |                |  |
| Interest income              | 5  | 7        | 32             | 19       |   |  |                |  |
| Interest expense             | (11 )  | —        | (127 )         | —        |   |  |                |  |
| Income before taxes          | \$2,971  | \$3,439  | \$7,259        | \$10,651 |   |  |                |  |

Intersegment sales are not material.

## Note 3 – Accounts receivable, net:

|                                 | December<br>31,<br>2013 | September<br>30,<br>2014 |
|---------------------------------|-------------------------|--------------------------|
|                                 | (In thousands)          |                          |
| Accounts receivable, net:       |                         |                          |
| Security Products               | \$7,813                 | \$10,334                 |
| Marine Components               | 849                     | 1,436                    |
| Allowance for doubtful accounts | (128 )                  | (130 )                   |
| Total accounts receivable, net  | \$8,534                 | \$11,640                 |

## Note 4 – Inventories, net:

|                         | December<br>31,<br>2013 | September<br>30,<br>2014 |
|-------------------------|-------------------------|--------------------------|
|                         | (In thousands)          |                          |
| <b>Raw materials:</b>   |                         |                          |
| Security Products       | \$2,565                 | \$ 2,543                 |
| Marine Components       | 1,000                   | 599                      |
| Total raw materials     | 3,565                   | 3,142                    |
| <b>Work-in-process:</b> |                         |                          |
| Security Products       | 5,992                   | 8,145                    |
| Marine Components       | 704                     | 1,526                    |
| Total work-in-process   | 6,696                   | 9,671                    |
| <b>Finished goods:</b>  |                         |                          |
| Security Products       | 2,349                   | 1,725                    |
| Marine Components       | 625                     | 544                      |
| Total finished goods    | 2,974                   | 2,269                    |
| Total inventories, net  | \$13,235                | \$ 15,082                |

## Note 5 – Other noncurrent assets:

|                               | December<br>31,<br>2013 | September<br>30,<br>2014 |
|-------------------------------|-------------------------|--------------------------|
|                               | (In thousands)          |                          |
| Assets held for sale          | \$532                   | \$ 588                   |
| Other                         | 41                      | 14                       |
| Total other noncurrent assets | \$573                   | \$ 602                   |

## Note 6 – Accounts payable and accrued liabilities:

|  | December<br>31,<br>2013 | September<br>30,<br>2014 |
|--|-------------------------|--------------------------|
|  | (In thousands)          |                          |
| Accounts payable                               | \$1,452                 | \$ 3,616                 |
| Accrued liabilities:                           |                         |                          |
| Employee benefits                              | 6,788                   | 6,036                    |
| Taxes other than on income                     | 378                     | 554                      |
| Customer tooling                               | 388                     | 426                      |
| Insurance                                      | 243                     | 215                      |
| Sales rebates                                  | 45                      | 204                      |
| Professional                                   | 86                      | 147                      |
| Other  | 325                     | 338                      |
| Total accounts payable and accrued liabilities | \$9,705                 | \$ 11,536                |

## Note 7 – Provision for income taxes:

Nine months  
ended  
September 30,  
2013 2014

(In thousands)

|   |         |         |
|---|---------|---------|
| Expected tax expense, at the U.S. federal statutory |         |         |
| income tax rate of 35%                              | \$2,541 | \$3,728 |
| State income taxes and other, net                   | 52      | (2 )    |
| Total income tax expense                            | \$2,593 | \$3,726 |

## Note 8 – Financial instruments:

The following table presents the financial instruments that are not carried at fair value but which require fair value disclosure:

|                           | December 31,<br>2013 |               | September 30,<br>2014 |               |
|---------------------------|----------------------|---------------|-----------------------|---------------|
|                           | Carrying<br>amount   | Fair<br>value | Carrying<br>amount    | Fair<br>value |
| (In thousands)            |                      |               |                       |               |
| Cash and cash equivalents | \$38,753             | \$38,753      | \$41,862              | \$41,862      |
| Accounts receivable, net  | 8,534                | 8,534         | 11,640                | 11,640        |
| Accounts payable          | 1,452                | 1,452         | 3,616                 | 3,616         |

Due to their near-term maturities, the carrying amounts of accounts receivable and accounts payable are considered equivalent to fair value.



Note 9 – Recent Accounting Pronouncements:

In May 2014, FASB issued Accounting Standards Update (“ASU”) No. 2014-09, Revenue from Contracts with Customers (Topic 606). This standard replaces existing revenue recognition guidance, which in many cases was tailored for specific industries, with a uniform accounting standard applicable to all industries and transactions. The new standard is effective for us beginning in the first quarter of 2017. Entities may elect to adopt ASU No. 2014-09 retrospectively for all periods for all contracts and transactions which occurred during the period (with a few exceptions for practical expediency) or retrospectively with a cumulative effect recognized as of the date of adoption. ASU No. 2014 is a fundamental rewriting of existing GAAP with respect to revenue recognition, and we are still evaluating the effect the Standard will have on our Consolidated Financial Statements. In addition, we have not yet determined the method we will use to adopt the Standard.

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

### Overview

We are a leading manufacturer of engineered components utilized in a variety of applications and industries. Through our Security Products segment we manufacture mechanical and electronic cabinet locks and other locking mechanisms used in recreational transportation, postal, office and institutional furniture, cabinetry, tool storage and healthcare applications. We also manufacture stainless steel exhaust systems, gauges and throttle controls for the recreational marine and other industries through our Marine Components segment.

We reported operating income of \$3.4 million in the third quarter of 2014 compared to \$3.0 million in the same period of 2013. We reported operating income of \$10.6 million for the nine month period ended September 30, 2014 compared to \$7.4 million for the comparable period in 2013. Our operating income increased for the quarter and for the nine month period in 2014 due to the positive impact of higher sales in 2014, primarily from an increase in Security Products sales to certain existing customers as well as increased market penetration in electronic locks.

Our product offerings consist of a significantly large number of products that have a wide variation in selling price and manufacturing cost, which results in certain practical limitations on our ability to quantify the impact of changes in individual product sales quantities and selling prices on our net sales, cost of goods sold and gross profit. In addition, small variations in period-to-period net sales, cost of goods sold and gross profit can result from changes in the relative mix of our products sold.

### Results of Operations

|                              | Three months ended<br>September 30, |        |          |        |
|------------------------------|-------------------------------------|--------|----------|--------|
|                              | 2013                                | %      | 2014     | %      |
|                              | (Dollars<br>in thousands)           |        |          |        |
| Net sales                    | \$24,209                            | 100.0% | \$26,473 | 100.0% |
| Cost of goods sold           | 16,695                              | 69.0%  | 18,331   | 69.2%  |
| Gross profit                 | 7,514                               | 31.0%  | 8,142    | 30.8%  |
| Operating costs and expenses | 4,537                               | 18.7%  | 4,710    | 17.8%  |
| Operating income             | \$2,977                             | 12.3%  | \$3,432  | 13.0%  |

|                              | Nine months ended<br>September 30, |        |          |        |
|------------------------------|------------------------------------|--------|----------|--------|
|                              | 2013                               | %      | 2014     | %      |
|                              | (Dollars<br>in thousands)          |        |          |        |
| Net sales                    | \$69,701                           | 100.0% | \$79,102 | 100.0% |
| Cost of goods sold           | 48,557                             | 69.7%  | 54,598   | 69.0%  |
| Gross profit                 | 21,144                             | 30.3%  | 24,504   | 31.0%  |
| Operating costs and expenses | 13,790                             | 19.8%  | 13,872   | 17.5%  |
| Operating income             | \$7,354                            | 10.6%  | \$10,632 | 13.4%  |

Net sales. Net sales increased \$2.3 million in the third quarter of 2014 and \$9.4 million in the first nine months of 2014 compared to the respective periods in 2013, led by strong demand within Security Products, including a new initiative for an existing government customer, increased market penetration in electronic locks and strong demand in transportation markets. Sales of Marine Components also contributed to the increase, reflecting greater penetration into non high-performance marine markets. Relative changes in selling prices did not have a material impact on net sales comparisons.

Cost of goods sold and gross profit. As a percentage of net sales, cost of goods sold for the third quarter of 2014 is comparable to the third quarter of 2013 as improved coverage of fixed manufacturing costs over increased production volumes was offset by the impact of a lower variable contribution margin due to relative changes in customer and product mix within Security Products. As a result, gross profit margin was comparable over the same period, while gross profit increased by \$628,000 on the higher sales. Cost of goods sold as a percentage of sales decreased by approximately 1% for the first nine months of 2014, primarily due to improved

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coverage of fixed manufacturing costs over increased production volumes to meet higher demand at each of our product segments, partially offset by the impact of lower variable margins due to relative changes in customer and product mix within Security Products and slightly increased medical expenses for the nine month period (most of which relates to the first half of the year). As a result, gross profit and related margin increased over the same period.

Operating costs and expenses. Operating costs and expenses consist primarily of sales and administrative related personnel costs, sales commissions and advertising expenses, as well as gains and losses on property, plant and equipment. Operating costs and expenses increased slightly for the third quarter and the first nine months of 2014 as compared to the same periods in 2013 primarily as a result of increased administrative personnel costs and increased depreciation for Security Products partially offset by reduced corporate administrative personnel cost.

Operating income. As a percentage of net sales, operating income increased by approximately 1% and 3% for the third quarter and first nine months of 2014 compared to the same periods in 2013, respectively. These increases were primarily the result of the factors impacting gross margin and operating costs and expenses above.

Provision for income taxes. A tabular reconciliation between our effective income tax rates and the U.S. federal statutory income tax rate of 35% is included in Note 7 to the Condensed Consolidated Financial Statements. Our operations are wholly within the U.S. and therefore our effective income tax rate is primarily reflective of the U.S. federal statutory rate.

#### Segment Results

The key performance indicator for our segments is operating income.

|                              | Three months ended<br>September 30, |          |        | % | Nine months ended<br>September 30, |          |        | % |
|------------------------------|-------------------------------------|----------|--------|---|------------------------------------|----------|--------|---|
|                              | 2013<br>(Dollars in<br>thousands)   | 2014     | Change |   | 2013<br>(Dollars in<br>thousands)  | 2014     | Change |   |
| <b>Net sales:</b>            |                                     |          |        |   |                                    |          |        |   |
| Security Products            | \$21,457                            | \$23,237 | 8      | % | \$61,258                           | \$69,246 | 13     | % |
| Marine Components            | 2,752                               | 3,236    | 18     | % | 8,443                              | 9,856    | 17     | % |
| Total net sales              | \$24,209                            | \$26,473 | 9      | % | \$69,701                           | \$79,102 | 13     | % |
| <b>Gross profit:</b>         |                                     |          |        |   |                                    |          |        |   |
| Security Products            | \$7,037                             | \$7,396  | 5      | % | \$19,476                           | \$22,222 | 14     | % |
| Marine Components            | 477                                 | 746      | 56     | % | 1,668                              | 2,282    | 37     | % |
| Total gross profit           | \$7,514                             | \$8,142  | 8      | % | \$21,144                           | \$24,504 | 16     | % |
| <b>Operating income:</b>     |                                     |          |        |   |                                    |          |        |   |
| Security Products            | \$4,578                             | \$4,694  | 3      | % | \$12,245                           | \$14,235 | 16     | % |
| Marine Components            | (17 )                               | 223      | 1,412  | % | 185                                | 729      | 294    | % |
| Corporate operating expenses | (1,584 )                            | (1,485 ) | 6      | % | (5,076 )                           | (4,332 ) | 15     | % |
| Total operating income       | \$2,977                             | \$3,432  | 15     | % | \$7,354                            | \$10,632 | 45     | % |
| <b>Gross profit margin:</b>  |                                     |          |        |   |                                    |          |        |   |
| Security Products            | 32.8                                | %        | 31.8   | % | 31.8                               | %        | 32.1   | % |
| Marine Components            | 17.3                                | %        | 23.1   | % | 19.8                               | %        | 23.2   | % |

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|                               |      |    |      |   |      |   |      |   |
|-------------------------------|------|----|------|---|------|---|------|---|
| Total gross profit margin     | 31.0 | %  | 30.8 | % | 30.3 | % | 31.0 | % |
| Operating income margin:      |      |    |      |   |      |   |      |   |
| Security Products             | 21.3 | %  | 20.2 | % | 20.0 | % | 20.6 | % |
| Marine Components             | (0.6 | )% | 6.9  | % | 2.2  | % | 7.4  | % |
| Total operating income margin | 12.3 | %  | 13.0 | % | 10.6 | % | 13.4 | % |

Security Products. Security Products net sales increased 8% in the third quarter and 13% in the first nine months of 2014 compared to the same periods last year. The increase in sales for the third quarter and nine month period is primarily due to increases of approximately \$1.1 million and \$4.0 million, respectively, in sales of new products for an existing government customer, \$1.0 million and \$3.3 million, respectively, to transportation market customers as a result of higher seasonal demand, and \$440,000 and \$1.8 million, respectively, to electronic lock customers in 2014 due to increased market penetration and two significant project installations.

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Gross profit margin for the third quarter of 2014 decreased 1% as compared to the same period in 2013 primarily due to relative changes in customer and product mix, resulting in lower variable margins, and increased fixed costs. Operating costs and expenses in the third quarter of 2014 increased approximately \$240,000 as compared to the third quarter of 2013, primarily as a result of an increase in administrative personnel and benefits costs and increased depreciation during the quarter. As a result, Security Products operating income as a percentage of net sales for the third quarter of 2014 decreased 1% as compared to the third quarter of 2013. Gross profit margin for the first nine months of 2014 is comparable to the same period in 2013 as improved coverage of fixed costs over increased production volumes were offset by lower variable margins and increased medical expenses of approximately \$241,000 over the nine month period. Additionally, operating costs and expenses for the first nine months of 2014 increased approximately \$760,000, primarily as a result of the increased administrative personnel and benefits costs of approximately \$310,000 and increased depreciation of approximately \$163,000 during 2014. Security Products operating income as a percentage of sales for the first nine months of 2014 is comparable to the first nine months of 2013 primarily as a result of factors impacting gross profit and operating costs and expenses discussed above.

Marine Components. Marine Components net sales increased 18% and 17% in the third quarter and first nine months of 2014, respectively, as compared to the same periods last year. The increase in sales is primarily due to gains in market share for products sold to the ski/wakeboard and other non high-performance marine markets. Gross margin and operating income percentage improved in the third quarter and for the first nine months of 2014 compared to the same periods in 2013 primarily due to improved variable margins related to product mix and increased leverage of fixed costs as a result of higher volumes.

Outlook. The robust demand for our products experienced through the first nine months of 2014 has been supported by seasonal influences and high demand from a number of our large government and commercial customers, offset by soft demand from small business customers. In addition, we continue to experience the benefits of diversification in our product offerings and ongoing innovation to serve new markets, most recently with our line of electronic locks for multiple high security applications. While seasonal demand will subside in the fourth quarter, we expect continued strong demand from our large government and commercial customers. As in prior periods, we will continue to monitor general economic conditions and sales order rates and respond to fluctuations in customer demand through continuous evaluation of staffing levels and consistent execution of our lean manufacturing and cost improvement initiatives.

Volatility in the costs of commodity raw materials is expected to continue. Our primary commodity raw materials are zinc, brass and stainless steel, which together represent approximately 11% of our total cost of goods sold. We generally seek to mitigate the impact of fluctuations in commodity raw material costs on our margins through improvements in production efficiencies or other operating cost reductions. In the event we are unable to offset commodity raw material cost increases with other cost reductions, it may be difficult to recover those cost increases through increased product selling prices or surcharges due to the competitive nature of the markets served by our products. Additionally, significant surcharges may negatively affect our margins as they typically only recover the increased cost of the raw material without adding margin dollars resulting in a lower margin percentage. Consequently, overall operating margins may be negatively affected by commodity raw material cost pressures.

#### Liquidity and Capital Resources

Consolidated cash flows –

Operating activities. Trends in cash flows from operating activities, excluding changes in assets and liabilities have generally been similar to the trends in operating earnings. Changes in assets and liabilities result primarily from the timing of production, sales and purchases. Changes in assets and liabilities generally tend to even out over time. However, period-to-period relative changes in assets and liabilities can significantly affect the comparability of cash flows from operating activities.

Our net cash provided by operating activities for the first nine months of 2014 increased by \$15.1 million as compared to the first nine months of 2013. The increase is primarily due to the net effects of:

The positive impact of lower net cash paid for taxes in 2014 of \$10.4 million primarily related to the previously-reported payment of income taxes in 2013 associated with the gain on sale of our disposed operations (\$11.6 million) recognized in the fourth quarter of 2012;

The positive impact of higher operating income in 2014 of \$3.3 million; and

The positive impact of lower net cash used by relative changes in our inventories, receivables, payables, and non-tax-related accruals of \$1.7 million.

Relative changes in working capital can have a significant effect on cash flows from operating activities. As shown below, the change in our average days sales outstanding from December 31, 2013 to September 30, 2014 varied by segment. Generally, we

expect our average days sales outstanding to increase from December to September as a result of seasonal increase in sales during the third quarter as compared to the fourth quarter. Overall, our September 30, 2014 days sales outstanding compared to December 31, 2013 is in line with our expectations. For comparative purposes, we have provided December 31, 2012 and September 30, 2013 numbers below.

| Days Sales Outstanding: | December 31, 2012 | September 30, 2013 | December 31, 2013 | September 30, 2014 |
|-------------------------|-------------------|--------------------|-------------------|--------------------|
| Security Products       | 41 Days           | 40 Days            | 35 Days           | 40 Days            |
| Marine Components       | 32 Days           | 37 Days            | 35 Days           | 39 Days            |
| Consolidated CompX      | 40 Days           | 40 Days            | 35 Days           | 40 Days            |

As shown below, our total average number of days in inventory on a consolidated basis decreased from December 31, 2013 to September 30, 2014 principally due to increased sales volumes in our Marine Components segments. Current Security Products inventories, relative to sales, are comparable to the beginning of the year, as increased sales volumes have offset inventory growth due to the introduction of new products and due to planned measures undertaken to avoid shortages of certain long lead-time components. The variability in days in inventory among our segments relates to the nature of the products and differences in the complexity of the production processes, which impact the length of time it takes to produce end-products. For comparative purposes, we have provided December 31, 2012 and September 30, 2013 numbers below.

| Days in Inventory: | December 31, 2012 | September 30, 2013 | December 31, 2013 | September 30, 2014 |
|--------------------|-------------------|--------------------|-------------------|--------------------|
| Security Products  | 71 Days           | 67 Days            | 71 Days           | 71 Days            |
| Marine Components  | 91 Days           | 91 Days            | 110 Days          | 98 Days            |
| Consolidated CompX | 74 Days           | 70 Days            | 76 Days           | 75 Days            |

Investing activities. Net cash used in investing activities was \$2.2 million in the first nine months of 2014 compared to net cash provided of \$1.9 million in the first nine months of 2013. Our capital expenditures in the first nine months of 2014 were \$2.2 million, slightly lower as compared to \$2.6 million in the first nine months of 2013. In addition, during 2013:

We collected \$3.0 million in principal payments on a note receivable; and  
 We received \$1.6 million in net proceeds on the sale of an asset held for sale.

Financing activities. Net cash used in financing activities was \$1.9 million in the first nine months of 2014 compared to net cash used of \$21.3 million in the first nine months of 2013. The change is primarily a result of the following items:

In 2013, we prepaid the remaining outstanding principal on our long-term debt, plus accrued interest, without penalty. Debt repayments related to principal for the first nine months of 2013 totaled \$18.5 million; and  
 Aggregate dividends we paid in the first nine months of 2014 were approximately \$930,000 lower as compared to the same period in 2013 as a result of reducing our regular quarterly dividend from \$0.125 per share to \$0.05 per share beginning in the second quarter of 2013.

Future cash requirements –

Liquidity. Our primary source of liquidity on an on-going basis is our cash flow from operating activities, which is generally used to (i) fund capital expenditures, (ii) repay short-term or long-term indebtedness incurred primarily for capital expenditures, investment activities or reducing our outstanding stock and (iii) provide for the payment of dividends (if declared). From time-to-time, we will incur indebtedness, primarily to fund capital expenditures or business combinations. In addition, from time-to-time, we may also sell assets outside the ordinary course of business,



the proceeds of which are generally used to repay indebtedness (including indebtedness which may have been collateralized by the assets sold) or to fund capital expenditures or business combinations.

Periodically, we evaluate liquidity requirements, alternative uses of capital, capital needs and available resources in view of, among other things, our capital expenditure requirements, dividend policy and estimated future operating cash flows. As a result of this process, we have in the past and may in the future seek to raise additional capital, refinance or restructure indebtedness, issue additional securities, modify our dividend policy or take a combination of such steps to manage our liquidity and capital resources. In the normal course of business, we may review opportunities for acquisitions, joint ventures or other business combinations in the component products industry. In the event of any such transaction, we may consider using available cash, issuing additional equity securities or increasing our indebtedness or that of our subsidiaries.

We believe that cash generated from operations together with cash on hand, as well as our ability to obtain external financing, will be sufficient to meet our liquidity needs for working capital, capital expenditures, debt service and dividends (if declared) for both the next 12 months and five years. To the extent that our actual operating results or other developments differ from our expectations, our liquidity could be adversely affected.

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All of our \$41.9 million aggregate cash and cash equivalents at September 30, 2014 were held in the U.S.

Capital Expenditures. Firm purchase commitments for capital projects in process at September 30, 2014 totaled \$508,000. Our 2014 capital investments are limited to those expenditures required to meet our expected customer demand and those required to properly maintain our facilities and technology infrastructure.

Commitments and Contingencies. There have been no material changes in our contractual obligations since we filed our 2013 Annual Report, and we refer you to that report for a complete description of these commitments.

Off-balance sheet financing arrangements –

We do not have any off-balance sheet financing agreements other than the operating leases discussed in our 2013 Annual Report.

Recent accounting pronouncements –

See Note 9 to our Condensed Consolidated Financial Statements.

Critical accounting policies –

There have been no changes in the first nine months of 2014 with respect to our critical accounting policies presented in Management's Discussion and Analysis of Financial Condition and Results of Operations in our 2013 Annual Report.

Forward-looking information –

As provided by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, we caution that the statements in this Quarterly Report on Form 10-Q relating to matters that are not historical facts are forward-looking statements that represent our beliefs and assumptions based on currently available information. Forward-looking statements can be identified by the use of words such as "believes," "intends," "may," "should," "anticipates," "expects" or comparable terminology, or by discussions of strategies or trends. Although we believe that the expectations reflected in such forward-looking statements are reasonable, we do not know if our expectations will prove to be correct. Such statements by their nature involve substantial risks and uncertainties that could significantly impact expected results, and actual future results could differ materially from those described in such forward-looking statements. Among the factors that could cause actual future results to differ materially are the risks and uncertainties discussed in this Quarterly Report and those described from time to time in our other filings with the Securities and Exchange Commission. While it is not possible to identify all factors, we continue to face many risks and uncertainties including, but not limited to the following:

- Future demand for our products,
- Changes in our raw material and other operating costs (such as zinc, brass and energy costs) and our ability to pass those costs on to our customers or offset them with reductions in other operating costs,
- Price and product competition from low-cost manufacturing sources (such as China),
- The impact of pricing and production decisions,
- Customer and competitor strategies including substitute products,
- Uncertainties associated with the development of new product features,
- Future litigation,
- Potential difficulties in integrating future acquisitions,
- Decisions to sell operating assets other than in the ordinary course of business,

Environmental matters (such as those requiring emission and discharge standards for existing and new facilities),  
The ultimate outcome of income tax audits, tax settlement initiatives or other tax matters,  
The impact of current or future government regulations (including employee healthcare benefit related regulations),  
Potential difficulties in upgrading or implementing new manufacturing and accounting software systems,  
General global economic and political conditions that introduce instability into the U.S. economy (such as changes in the level of gross domestic product in various regions of the world),

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Operating interruptions (including, but not limited to labor disputes, hazardous chemical leaks, natural disasters, fires, explosions, unscheduled or unplanned downtime, transportation interruptions and cyber attacks); and Possible disruption of our business or increases in the cost of doing business resulting from terrorist activities or global conflicts.

Should one or more of these risks materialize or if the consequences worsen, or if the underlying assumptions prove incorrect, actual results could differ materially from those currently forecasted or expected. We disclaim any intention or obligation to update or revise any forward-looking statement whether as a result of changes in information, future events or otherwise.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

We are exposed to market risk from changes in interest rates and raw material prices. There have been no material changes in these market risks since we filed our 2013 Annual Report, and we refer you to Part I, Item 7A – “Quantitative and Qualitative Disclosure About Market Risk” in our 2013 Annual Report. See also Note 8 to the Condensed Consolidated Financial Statements.

### ITEM 4. CONTROLS AND PROCEDURES.

**Evaluation of Disclosure Controls and Procedures.** We maintain a system of disclosure controls and procedures. The term “disclosure controls and procedures,” as defined by regulations of the SEC, means controls and other procedures that are designed to ensure that information required to be disclosed in the reports that we file or submit to the SEC under the Securities Exchange Act of 1934, as amended (the “Act”), is recorded, processed, summarized and reported, within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information we are required to disclose in the reports that we file or submit to the SEC under the Act is accumulated and communicated to our management, including our principal executive officer and our principal financial officer, or persons performing similar functions, as appropriate to allow timely decisions to be made regarding required disclosure. Our management with the participation of David A. Bowers, our Vice Chairman of the Board and Chief Executive Officer, and James W. Brown, our Vice President, Chief Financial Officer and Controller, have evaluated the design and operating effectiveness of our disclosure controls and procedures as of September 30, 2014. Based upon their evaluation, these executive officers have concluded that our disclosure controls and procedures are not effective as of the date of such evaluation because of the material weakness in our internal control over financial reporting described below.

**Internal Control Over Financial Reporting.** We also maintain internal control over financial reporting. The term “internal control over financial reporting,” as defined by regulations of the SEC, means a process designed by, or under the supervision of, our principal executive and principal financial officers, or persons performing similar functions, and effected by our board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP, and includes those policies and procedures that:

- pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of our assets,
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors, and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on our Condensed Consolidated Financial Statements.

A material weakness is a deficiency or a combination of deficiencies in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis.

**Status of Remediation of Material Weakness.** As disclosed in our June 30, 2014 Form 10-Q, during the first quarter of 2014, we implemented a new enterprise resource planning (“ERP”) system covering financial, production and logistics processes. We concluded that, from the date of implementation through June 30, 2014, we did not maintain effective monitoring controls over user access to the new ERP system, which constitutes a material weakness. Specifically, within the new ERP system we did not maintain information technology and business process controls over evaluating and monitoring user access rights and transactions processed for appropriate segregation of duties including producing reports to monitor activity related to the appropriateness of access. We have taken the following steps to remediate the identified material weakness. Since June 30, 2014, we have implemented control

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procedures, including information technology and business process controls, to address management's ability to evaluate and effectively monitor user access rights and segregation of duties. We believe these additional control procedures have strengthened our internal controls over financial reporting and addressed the material weakness. Testing of the effectiveness of these controls has begun and we expect such testing to be completed during the fourth quarter of 2014. Once testing has been completed and we have concluded that the remediation measures described above are in place and operating effectively, we will be able to conclude that the material weakness has been remediated. We will continue to test and evaluate these controls as part of our 2014 assessment of internal controls over financial reporting.

**Changes in Internal Control Over Financial Reporting.** Other than the implementation of additional control procedures noted above, there have been no changes in our internal control over financial reporting during the quarter ended September 30, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Part II. OTHER INFORMATION

ITEM 1A. Risk Factors.

Reference is made to the 2013 Annual Report for a discussion of the risk factors related to our businesses. There have been no material changes in such risk factors during the first nine months of 2014.

ITEM 6. Exhibits.

| Item No. | Exhibit Index                                 |
|----------|---|
| 31.1     | Certification                                 |
| 31.2     | Certification                                 |
| 32.1     | Certification                                 |
| 101.INS  | XBRL Instance Document                        |
| 101.SCH  | XBRL Taxonomy Extension Schema                |
| 101.CAL  | XBRL Taxonomy Extension Calculation Linkbase  |
| 101.DEF  | XBRL Taxonomy Extension Definition Linkbase   |
| 101.LAB  | XBRL Taxonomy Extension Label Linkbase        |
| 101.PRE  | XBRL Taxonomy Extension Presentation Linkbase |

We have retained a signed original of any of the above exhibits that contains signatures, and we will provide such exhibit to the Commission or its staff upon request. We will also furnish, without charge, a copy of our Code of Business Conduct and Ethics, and Audit Committee Charter, each as adopted by our board of directors on February 22, 2012 and March 2, 2011 respectively, upon request. Such requests should be directed to the attention of our Corporate Secretary at our corporate offices located at 5430 LBJ Freeway, Suite 1700, Dallas, Texas 75240.





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.

COMPX INTERNATIONAL INC.  
(Registrant)

Date: November 5, 2014 By: /s/ James W. Brown  
James W. Brown  
Vice President, Chief Financial Officer and Controller