

BADGER METER INC
Form 10-Q
April 23, 2009

Table of Contents

**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 March 31, 2009**

**BADGER METER, INC.
4545 W. Brown Deer Road
Milwaukee, Wisconsin 53223
(414) 355-0400**

A Wisconsin Corporation
IRS Employer Identification No. 39-0143280
Commission File No. 001-6706

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). (Registrant is not yet required to provide financial disclosure in an Interactive Data File format.) Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definitions of large accelerated filer, accelerated filer and smaller reporting 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

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

As of April 10, 2009, there were 14,812,889 shares of Common Stock outstanding with a par value of \$1 per share.

BADGER METER, INC.
Quarterly Report on Form 10-Q for Period Ended March 31, 2009
Index

	Page No.
<u>Part I. Financial Information:</u>	
<u>Item 1</u>	<u>Financial Statements:</u>
	<u>Consolidated Condensed Balance Sheets - March 31, 2009 and December 31, 2008</u>
	4
	<u>Consolidated Condensed Statements of Operations - Three Months Ended March 31, 2009 and 2008</u>
	5
	<u>Consolidated Condensed Statements of Cash Flows - Three Months Ended March 31, 2009 and 2008</u>
	6
	<u>Notes to Unaudited Consolidated Condensed Financial Statements</u>
	7
<u>Item 2</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>
	9
<u>Item 3</u>	<u>Quantitative and Qualitative Disclosures about Market Risk</u>
	13
<u>Item 4</u>	<u>Controls and Procedures</u>
	13
<u>Part II. Other Information:</u>	
<u>Item 6</u>	<u>Exhibits</u>
	13
<u>Signatures</u>	14
<u>Exhibit Index</u>	15
<u>EX-31.1</u>	
<u>EX-31.2</u>	
<u>EX-32</u>	

Table of Contents

Special Note Regarding Forward Looking Statements

Certain statements contained in this Quarterly Report on Form 10-Q, as well as other information provided from time to time by Badger Meter, Inc. (the Company) or its employees, may contain forward looking statements that involve risks and uncertainties that could cause actual results to differ materially from those in the forward looking statements. The words anticipate, believe, estimate, expect, think, should, could and objective or similar are intended to identify forward looking statements. All such forward looking statements are based on the Company's then current views and assumptions and involve risks and uncertainties that include, among other things:

the continued shift in the Company's business from lower cost, manually read meters toward more expensive, value-added automatic meter reading (AMR) systems and advanced metering infrastructure (AMI) systems;

the success or failure of newer Company products, including the Orion® radio frequency AMR system, the Galaxy® fixed network AMI system and the low profile Recordall® Model LP disc series meter;

changes in competitive pricing and bids in both the domestic and foreign marketplaces, and particularly in continued intense price competition on government bid contracts for lower cost, manually read meters;

the actions (or lack thereof) of the Company's competitors;

changes in the Company's relationships with its alliance partners, primarily its alliance partners that provide AMR/AMI connectivity solutions, and particularly those that sell products that do or may compete with the Company's products;

changes in the general health of the United States and foreign economies, including to some extent such things as the length and severity of the current global economic downturn, the ability of municipal water utility customers to authorize and finance purchases of the Company's products, the Company's ability to obtain financing, housing starts in the United States, and overall industrial activity;

changes in the cost and/or availability of needed raw materials and parts, including recent volatility in the cost of brass castings as a result of fluctuations in commodity prices, particularly for copper and scrap metal, at the supplier level and plastic resin as a result of changes in petroleum and natural gas prices;

the Company's expanded role as a prime contractor for providing complete AMR/AMI systems to governmental entities, which brings with it added risks, including but not limited to, Company responsibility for subcontractor performance, additional costs and expenses if the Company and its subcontractors fail to meet the agreed-upon timetable with the governmental entity, and the Company's expanded warranty and performance obligations;

changes in foreign economic conditions, particularly currency fluctuations in the United States dollar, the euro and the peso;

the loss of certain single-source suppliers; and

changes in laws and regulations, particularly laws dealing with the use of lead (which can be used in the manufacture of certain meters incorporating brass housings) and the U.S. Federal Communications Commission rules affecting the use and/or licensing of radio frequencies necessary for AMR/AMI products.

All of these factors are beyond the Company's control to varying degrees. Shareholders, potential investors and other readers are urged to consider these factors carefully in evaluating the forward looking statements and are cautioned not to place undue reliance on such forward looking statements. The forward looking statements made in this document are made only as of the date of this document and the Company assumes no obligation, and disclaims

any obligation, to update any such forward looking statements to reflect subsequent events or circumstances.

Table of Contents**Part I Financial Information****Item 1 Financial Statements****BADGER METER, INC.
Consolidated Condensed Balance Sheets**

	March 31, 2009 (Unaudited)	December 31, 2008
	(In thousands)	
Assets		
Current assets:		
Cash	\$ 6,090	\$ 6,217
Receivables	34,745	35,767
Inventories:		
Finished goods	13,455	13,484
Work in process	10,895	10,990
Raw materials	15,701	14,841
Total inventories	40,051	39,315
Prepaid expenses and other current assets	3,878	2,316
Deferred income taxes	2,903	2,914
Total current assets	87,667	86,529
Property, plant and equipment, at cost	134,969	133,934
Less accumulated depreciation	(73,771)	(72,111)
Net property, plant and equipment	61,198	61,823
Intangible assets, at cost less accumulated amortization	24,673	25,030
Other assets	5,736	5,713
Deferred income taxes	9,306	9,305
Goodwill	6,958	6,958
Total assets	\$ 195,538	\$ 195,358
Liabilities and shareholders equity		
Current liabilities:		
Short-term debt	\$ 5,593	\$ 9,995
Current portion of long-term debt	9,800	9,675
Payables	14,333	13,230
Accrued compensation and employee benefits	6,177	8,714
Warranty and after-sale costs	1,384	1,327
Income and other taxes	9,968	7,848
Total current liabilities	47,255	50,789

Edgar Filing: BADGER METER INC - Form 10-Q

Other long-term liabilities	1,038	1,059
Deferred income taxes	121	133
Accrued non-pension postretirement benefits	5,719	5,585
Other accrued employee benefits	21,673	21,265
Long-term debt	2,930	5,504
Commitments and contingencies (Note 6)		
Shareholders' equity:		
Common stock	21,083	21,074
Capital in excess of par value	31,923	31,563
Reinvested earnings	113,236	107,887
Accumulated other comprehensive loss	(16,693)	(16,672)
Less: Employee benefit stock	(585)	(659)
Treasury stock, at cost	(32,162)	(32,170)
Total shareholders' equity	116,802	111,023
Total liabilities and shareholders' equity	\$ 195,538	\$ 195,358

See accompanying notes to consolidated condensed financial statements.

Table of Contents

BADGER METER, INC.
Consolidated Condensed Statements of Operations

	Three Months Ended March 31, (Unaudited)	
	2009	2008
	(In thousands except share and per share amounts)	
Net sales	\$ 65,324	\$ 68,420
Cost of sales	39,152	43,896
Gross margin	26,172	24,524
Selling, engineering and administration	14,704	14,655
Operating earnings	11,468	9,869
Interest expense	400	252
Earnings before income taxes	11,068	9,617
Provision for income taxes	4,095	3,597
Net earnings	\$ 6,973	\$ 6,020
Earnings per share amounts:		
Basic	\$ 0.47	\$ 0.42
Diluted	\$ 0.47	\$ 0.41
Dividends declared	\$ 0.11	\$ 0.09
Shares used in computation of earnings per share:		
Basic	14,689,324	14,394,862
Impact of dilutive securities	191,176	355,374
Diluted	14,880,500	14,750,236

See accompanying notes to consolidated condensed financial statements.

Table of Contents

BADGER METER, INC.
Consolidated Condensed Statements of Cash Flows

	Three Months Ended March 31, (Unaudited) (In thousands)	
	2009	2008
Operating activities:		
Net earnings	\$ 6,973	\$ 6,020
Adjustments to reconcile net earnings to net cash provided by (used for) operations:		
Depreciation	1,660	1,770
Amortization	357	27
Deferred income taxes	3	13
Noncurrent employee benefits	971	861
Stock-based compensation expense	320	305
Changes in:		
Receivables	776	(2,919)
Inventories	(836)	(4,153)
Prepaid expenses and other current assets	(1,618)	(1,174)
Current liabilities other than debt	622	3,783
Total adjustments	2,255	(1,487)
Net cash provided by operations	9,228	4,533
Investing activities:		
Property, plant and equipment additions	(1,305)	(2,781)
Other net	(69)	(140)
Net cash used for investing activities	(1,374)	(2,921)
Financing activities:		
Net decrease in short-term debt	(4,248)	(3,221)
Repayments of long-term debt	(2,449)	(526)
Dividends paid	(1,621)	(1,303)
Proceeds from exercise of stock options	75	531
Tax benefit on stock options	46	810
Issuance of treasury stock	42	37
Net cash used for financing activities	(8,155)	(3,672)
Effect of foreign exchange rates on cash	174	(324)
Decrease in cash	(127)	(2,384)

Cash	beginning of period	6,217	8,670
Cash	end of period	\$ 6,090	\$ 6,286

See accompanying notes to consolidated condensed financial statements.

6

Table of Contents**BADGER METER, INC.****Notes to Unaudited Consolidated Condensed Financial Statements****Note 1 Basis of Presentation**

In the opinion of management, the accompanying unaudited consolidated condensed financial statements of Badger Meter, Inc. (the Company) contain all adjustments (consisting only of normal recurring accruals except as otherwise discussed) necessary to present fairly the Company's consolidated condensed financial position at March 31, 2009, results of operations for the three-month periods ended March 31, 2009 and 2008, and cash flows for the three-month periods ended March 31, 2009 and 2008. The results of operations for any interim period are not necessarily indicative of the results to be expected for the full year.

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Note 2 Additional Balance Sheet Information

The consolidated condensed balance sheet at December 31, 2008 was derived from amounts included in the Company's Annual Report on Form 10-K for the year ended December 31, 2008. Refer to the footnotes to the financial statements included in that report for a description of the Company's accounting policies and for additional details of the Company's financial condition. The details in those notes have not changed except as discussed below and as a result of normal adjustments in the interim.

Warranty and After-Sale Costs

The Company estimates and records provisions for warranties and other after-sale costs in the period in which the sale is recorded, based on a lag factor and historical warranty claim experience. After-sale costs represent a variety of activities outside of the written warranty policy, such as investigation of unanticipated problems after the customer has installed the product, or analysis of water quality issues. Changes in the Company's warranty and after-sale costs reserve for the three-month periods ended March 31, 2009 and 2008 are as follows:

(In thousands)	Balance at beginning of year	Net additions charged to earnings	Costs incurred and adjustments	Balance at March 31
2009	\$ 1,327	\$ 193	\$ (136)	\$ 1,384
2008	\$ 1,917	\$ 319	\$ (280)	\$ 1,956

Note 3 Employee Benefit Plans

The Company maintains a non-contributory defined benefit pension plan for its domestic employees and a non-contributory postretirement plan that provides medical benefits for certain domestic retirees and eligible dependents. The following table sets forth the components of net periodic benefit cost for the three months ended March 31, 2009 and 2008 based on December 31, 2008 and 2007 measurement dates, respectively:

(In thousands)	Pension benefits		Other postretirement benefits	
	2009	2008	2009	2008
Service cost - benefits earned during the year	\$ 487	\$ 493	\$ 33	\$ 37
Interest cost on projected benefit obligations	763	686	101	101
Expected return on plan assets	(847)	(864)		
Amortization of prior service cost (credit)	(16)	(36)	45	45

Edgar Filing: BADGER METER INC - Form 10-Q

Amortization of net loss	267	290		8
Net periodic benefit cost	\$ 654	\$ 569	\$ 179	\$ 191

7

Table of Contents

The Company previously disclosed in its financial statements for the year ended December 31, 2008 that it anticipated making a contribution of \$4.9 million to its pension plan in 2009 due to the reduction in the market value of the underlying investments as of the December 31, 2008 actuarial measurement date. However, this estimate is subject to further calculations prior to the actual payment.

The Company disclosed in its financial statements for the year ended December 31, 2008 that it estimated it would pay \$0.6 million in other postretirement benefits in 2009 based on actuarial estimates. As of March 31, 2009, an immaterial amount of such benefits was paid. The Company now believes that its estimated payments for the full year may be somewhat less than the prior full-year estimate. However, such estimates contain inherent uncertainties because cash payments can vary significantly depending on the timing of postretirement medical claims and the collection of the retiree's portion of certain costs. Note that the amount of benefits paid in calendar year 2009 will not impact the expense for postretirement benefits for the current year.

Note 4 Guarantees

The Company guarantees the outstanding debt of the Badger Meter Employee Savings and Stock Ownership Plan (ESSOP) that is recorded in long-term debt, offset by a similar amount of unearned compensation that has been recorded as a reduction of shareholders' equity. The loan amount is collateralized by shares of the Company's Common Stock. A payment of \$74,000 was made in the first quarter of 2009 that reduced the debt and the corresponding employee benefit stock balance included in shareholders' equity.

Note 5 Comprehensive Income (Loss)

Comprehensive income for the three-month periods ended March 31, 2009 and 2008 was \$7.0 million and \$6.7 million, respectively.

Components of accumulated other comprehensive loss are as follows:

(In thousands)	March 31, 2009	December 31, 2008
Cumulative foreign currency translation adjustment	\$ 1,416	\$ 1,639
Unrecognized pension and postretirement benefit plan liabilities (net of tax of \$11.0 million and \$11.2 million for 2009 and 2008, respectively)	(18,109)	(18,311)
Accumulated other comprehensive loss	\$ (16,693)	\$ (16,672)

Note 6 Contingencies, Litigation and Commitments

In the normal course of business, the Company is named in legal proceedings. There are currently no material legal proceedings pending with respect to the Company. The more significant legal proceedings are discussed below.

The Company is subject to contingencies related to environmental laws and regulations. Currently, the Company is in the process of resolving matters relating to two landfill sites where it has been named as one of many potentially responsible parties and to a parcel of land adjoining the Company's property. The landfill sites are impacted by the Federal Comprehensive Environmental Response, Compensation and Liability Act and other environmental laws and regulations. At this time, the Company does not believe the ultimate resolution of these issues will have a material adverse effect on the Company's financial position or results of operations, either from a cash flow perspective or on the financial statements as a whole. This belief is based on the Company's assessment of its limited past involvement with these landfill sites as well as the substantial involvement of other named third parties with these landfill sites. However, due to the inherent uncertainties of such proceedings, the Company cannot predict the ultimate outcome of these matters. A future change in circumstances with respect to these specific matters or with respect to sites formerly or currently owned or operated by the Company, or with respect to off-site disposal locations used by the Company, could result in future costs to the Company and such amounts could be material. Expenditures during 2008 and the first quarter of 2009 were not material for compliance with environmental control provisions and regulations.

Like other companies in recent years, the Company has been named as a defendant in numerous multi-claimant/multi-defendant lawsuits alleging personal injury as a result of exposure to asbestos, manufactured by third parties, and integrated into or sold with a very limited number of the Company's products. The Company is vigorously defending itself against these claims. Although it is not possible to predict the ultimate outcome of

Table of Contents

these matters, the Company does not believe the ultimate resolution of these issues will have a material adverse effect on the Company's financial position or results of operations, either from a cash flow perspective or on the financial statements as a whole. This belief is based in part on the fact that no claimant has demonstrated exposure to products manufactured or sold by the Company and that a number of cases have been voluntarily dismissed.

The Company relies on single suppliers for certain castings and components in several of its product lines. Although alternate sources of supply exist for these items, loss of certain suppliers could temporarily disrupt operations in the short term. The Company attempts to mitigate these risks by working closely with key suppliers, purchasing minimal amounts from alternative suppliers and by purchasing business interruption insurance where appropriate.

The Company reevaluates its exposures on a periodic basis and makes adjustments to reserves as appropriate.

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

Business Description and Overview

The Company is a leading manufacturer and marketer of products incorporating liquid flow measurement and control technologies, developed both internally and in conjunction with other technology companies. Its products are used in a wide variety of applications to measure and control the flow of liquids, but primarily water. The Company's product lines fall into two general categories, utility and industrial. The utility category is comprised of two primary product lines—residential and commercial water meters that are used by water utilities as the basis for generating water and wastewater revenues. The market for these product lines is North America, primarily the United States, because these meters are designed and manufactured to conform to standards promulgated by the American Water Works Association. The utility flow measurement products constitute a majority of the Company's sales.

Industrial product line sales comprise the remainder of the Company's sales and include precision valves, electromagnetic inductive flow meters, impeller flow meters, and turbine and positive displacement industrial flow meters. Rounding out the industrial product line are automotive fluid meters used for the measurement of various types of automotive fluids.

Residential and commercial water meters have generally been classified as either manually read meters or remotely read meters via radio technology. A meter that is manually read consists of the water meter and a register that gives a visual display of the meter reading. Meters equipped with radio transmitters convert the mechanical measurement to a digital format which is then transmitted via radio frequency to a receiver that collects and formats the data appropriately for a water utility's billing computer. Drive-by systems are referred to as automatic meter reading (AMR) systems and have been the primary technology deployed by water utilities over the past decade, providing cost effective and accurate billing data. In a drive-by AMR system, a vehicle equipped for meter reading purposes, including a radio receiver and computer, collects meter reading data.

Of growing interest to water utilities are fixed network advanced metering infrastructure (AMI) systems. These systems do not rely on a drive-by data collector, but rather incorporate a network of permanent radio receivers or data collectors that are always active or listening to the radio transmission from the utility's meters. Not only do fixed network systems eliminate the need for meter readers, but they have the ability to provide the utility with more frequent and diverse data at specified intervals. The Company's response to these market requirements is detailed further in the Business Trends section.

The Company's net sales and corresponding net earnings depend on unit volume and mix of products, with the Company generally earning higher margins on meters equipped with AMR or AMI technology. In addition to selling its proprietary AMR/AMI products, including the Orion® drive-by AMR technology and the Galaxy® fixed network AMI system, the Company also remarkets the Itron® drive-by AMR product under a license and distribution agreement. The Company's proprietary AMR/AMI products generally result in higher margins than the non-proprietary AMR/AMI products that the Company remarkets. The Company also sells registers and radios separately to customers who wish to perform a field upgrade of their existing meters.

One distinctive advantage of the Orion® AMR technology is that while it is fundamentally a drive-by AMR system, the proprietary receiver technology of Orion® has been licensed to other technology providers, including those providing AMR/AMI products that communicate over power lines, broadband networks, and proprietary

Table of Contents

radio frequency networks. In addition, the Company produces a universal gateway receiver for Orion® that enables Orion® AMR data to be transmitted to a utility customer over a variety of public wireless networks.

The sales of utility flow measurement products, including AMR/AMI product sales, are generally derived from the water meter replacement requirements of customers, along with their plans for adoption and deployment of new technology. To a much lesser extent, housing starts also contribute to the base of new product sales. Over the last decade there has been a growing trend in the conversion to AMR/AMI from manually read water meters. This conversion rate is accelerating and contributing to an increased base of business available to meter and AMR/AMI producers. It is currently estimated that less than 30% of water meters installed in the United States have been converted to AMR/AMI systems. The Company's strategy is to fulfill customers' metering expectations and requirements with its proprietary meter reading systems or other systems available through its alliance partners in the marketplace.

The industrial products generally serve a variety of niche flow measurement applications across a broad range of industries. For instance, the impeller product line is widely used in irrigation, HVAC and fire prevention equipment. Some of the flow measurement technologies used for industrial applications have been derived from utility meter technologies, such as positive displacement and turbine flow measurement. Other technologies are very specific to industrial applications. In addition, a growing requirement is for industrial meters to be equipped with specialized communication protocols that control the entire flow measurement process. Serving both the utility and industrial flow measurement market enables the Company to use its wide variety of technology for specific flow measurement and control applications, as well as to utilize existing capacity and spread fixed costs over a larger sales base.

Business Trends

AMI is the growing standard of technology deployment in the electric utility industry. AMI provides an electric utility with two-way communication to monitor and control electrical devices at the customer's site. AMI deployments are fixed network technologies. Although the Company does not participate in the electric market, the trend toward AMI is now affecting the markets the Company does participate in, namely water and gas utility markets. Specifically, in the water industry, fixed network AMI enables the water utility to capture interval readings from each meter on a daily basis. While two-way communication is currently limited in water fixed network AMI, utilities are contemplating how two-way networks could benefit them. As noted above, the Company markets the Orion® drive-by AMR product line as well as the Galaxy® fixed network AMI product line. The Company is positioned to sell either product in responding to customer requirements. Since both products have comparable margins, any acceleration or slowdown in this trend is not expected to have a significant impact on the Company.

Although there is growing interest in fixed network communication by water utilities, the vast majority of utilities currently installing AMR/AMI continue to select drive-by AMR technologies for their applications. The Company's Orion® technology has experienced rapid acceptance in the United States. By the end of 2008, an increasing number of water utilities had selected Orion® as their AMR solution of choice. There are approximately 53,000 water utilities in the United States and the Company estimates that less than 30% of them have converted to an AMR or AMI technology. The Company anticipates that even with growing interest in fixed network AMI, drive-by AMR will continue to be the primary product of choice by water utilities for a number of years. Drive-by AMR technology is simply the most cost effective form of AMR currently available to water utilities.

Revenue and Product Mix

Prior to the Company's introduction of its own proprietary Orion® products, Itron® water utility-related products were a dominant AMR contributor to the Company's results. Itron® products are sold under an agreement between the Company and Itron, Inc. that expires in early 2011. The Company's Orion® products directly compete with Itron® water AMR products and, in recent years, many of the Company's customers have selected Orion® products. While Orion® sales were 2.4 times greater than those of the Itron® licensed products for the full year of 2008, the Company expects that the Itron® products will remain a significant component of utility sales. The increases in both product lines underscores the continued acceptance of the AMR technology by water utilities and affirms the Company's strategy of selling Itron® products in addition to its own proprietary products.

As the industry continues to evolve, there may be additional opportunities for revenue enhancement. For instance, in recent years the Company has been asked to oversee and perform installation of its products in the field

for a limited number of customers. This is usually accomplished by the Company assuming the role of

Table of Contents

the general contractor, hiring a subcontractor and supervising their work. The Company also sells certain extended warranty programs for the technology sold with meters. The extended warranties provide additional services beyond the one-year standard warranty. In 2008, the Company also began to sell the Orion® technology to natural gas utilities for installation on their gas meters. Revenues for all of these types of products and services are not yet significant and the Company is uncertain of the potential growth achievable for these products in future periods.

Results of Operations Three Months Ended March 31, 2009

Net sales for the three months ended March 31, 2009 decreased \$3.1 million, or 4.5%, to \$65.3 million from \$68.4 million in the same period in 2008. The decrease was driven by lower sales of the Company's industrial products, partially offset by a small increase in sales of its utility products.

Residential and commercial water meter and related AMR/AMI sales represented 86.0% of total net sales for the quarter compared to 81.2% in the first quarter of 2008. These sales were \$56.2 million, an increase of \$0.7 million, or 1.3%, from \$55.5 million in the same period in 2008. This increase was the net result of a 9.3% increase in residential sales, including Orion®, Itron® and Galaxy® technologies and related parts, and a 28.3% decrease in commercial sales driven by lower volumes. Sales of the Company's proprietary AMR product, Orion®, increased 7.7% on slightly lower volumes while sales of the remarketed Itron® product increased by 13.1%. The Orion® products outsold the Itron® products by a ratio of nearly 2.7 to 1 for the three-month period ended March 31, 2009.

Industrial sales represented 14.0% of the total net sales for the quarter ended March 31, 2009 compared to 18.8% for the same period in 2008. Industrial sales were \$9.1 million in the first quarter of 2009, a decrease of 29.5% over sales of \$12.9 million in the same period in 2008. This decrease was due to lower sales volumes in all product lines of this group as a result of the weaker economy, mitigated somewhat by price increases in several of the lines. Sales of the Company's industrial products generally fluctuate with the condition of the overall economy.

The total gross margin percentage increased in the first quarter of 2009 to 40.1% from 35.8% for the same period in 2008. The increase was primarily due to the favorable effects of lower raw material costs, including meter castings that fluctuate with the metals market, and radio purchases that are sourced in Europe that benefitted from the strengthening of the U.S. dollar.

Selling, engineering and administration costs were relatively flat at \$14.7 million in both the three months ended March 31, 2009 and 2008. This was the net effect of lower costs associated with lower sales and favorable health care costs, offset by increased amortization related to the acquisition of the North American rights for the Galaxy® fixed network technology in the second quarter of 2008. In addition, the first quarter of 2009 included charges associated with early retirement programs offered to certain U.S. employees. The first quarter of 2008 included costs related to efforts to establish a presence for Orion® in the natural gas industry that did not reoccur in the first quarter of 2009. The Company also experienced normal inflationary increases in 2009, which were somewhat offset by continuing cost containment efforts.

The provision for income taxes as a percentage of earnings before income taxes for the first quarter of 2009 was 37.0% compared to 37.4% for the same period in 2008.

As a result of the above mentioned items, net earnings were \$7.0 million for the three months ended March 31, 2009 compared to \$6.0 million for the three months ended March 31, 2008. On a diluted basis, earnings per share were \$0.47 for the first quarter of 2009 compared to \$0.41 for the same period in 2008.

Liquidity and Capital Resources

The main sources of liquidity for the Company are cash from operations and borrowing capacity. Cash provided by operations for the first three months of 2009 was \$9.2 million compared to \$4.5 million for the same period in 2008. The increase was due to the increase in earnings and maintaining inventories and receivables at comparable levels to the 2008 year-end balances compared to the first quarter of 2008 when they increased significantly from the 2007 year-end levels.

The decrease in the receivables balance from \$35.8 million at December 31, 2008 to \$34.7 million at March 31, 2009 was due primarily to the lower sales, the timing of those sales and certain cash collections. The Company continues to believe that recent financial concerns in the overall economy will not impact collections of these receivables.

Table of Contents

Inventories at March 31, 2009 increased to \$40.1 million from \$39.3 million at December 31, 2008 due primarily to lower than expected industrial sales and the timing of purchases.

Prepaid expenses and other current assets at March 31, 2009 increased to \$3.9 million from \$2.3 million at December 31, 2008 primarily due to the payment of certain calendar year insurance premiums that are expensed ratably over the policy period.

Net property, plant and equipment at March 31, 2009 decreased by \$0.6 million since December 31, 2008 as the result of \$1.3 million of capital expenditures, offset by depreciation expense.

Short-term debt at March 31, 2008 decreased by \$4.4 million compared to the balance at December 31, 2008 as cash provided from operations was used to pay down these amounts. During the same period, long-term debt, including current maturities decreased \$2.4 million on a net basis due to regularly scheduled payments. All of the Company's debt is unsecured and does not carry any financial covenants.

Payables increased to \$14.3 million at March 31, 2009 from \$13.2 million at December 31, 2008 primarily due to the timing of payments. Accrued compensation and employee benefits at March 31, 2009 decreased to \$6.2 million from \$8.7 million at December 31, 2008 due to the payment of employee incentive amounts accrued at December 31, 2008, offset somewhat by current year accruals.

Accrued income and other taxes increased to \$10.0 million at March 31, 2009 from \$7.8 million at December 31, 2008 due to increased earnings and the timing of income tax payments.

Common stock and capital in excess of par value both increased since December 31, 2008 due to new stock issued in connection with the exercise of stock options. Employee benefit stock decreased as a result of a payment made on the Badger Meter Employee Savings and Stock Ownership Plan loan during the first quarter of 2009.

The Company believes its financial condition remains strong. In October 2008, the Company renewed its principal line of credit (\$30.0 million) for one year with its primary lender. The Company believes that its operating cash flows, available borrowing capacity, and its ability to raise capital provide adequate resources to fund ongoing operating requirements, future capital expenditures and development of new products. The Company has \$39.7 million of unused credit lines available at March 31, 2009.

Other Matters

There are currently no material legal proceedings pending with respect to the Company. The more significant legal proceedings are discussed below.

The Company is subject to contingencies related to environmental laws and regulations. Currently, the Company is in the process of resolving matters relating to two landfill sites where it has been named as one of many potentially responsible parties and to a parcel of land adjoining the Company's property. The landfill sites are impacted by the Federal Comprehensive Environmental Response, Compensation and Liability Act and other environmental laws and regulations. At this time, the Company does not believe the ultimate resolution of these issues will have a material adverse effect on the Company's financial position or results of operations, either from a cash flow perspective or on the financial statements as a whole. This belief is based on the Company's assessment of its limited past involvement with these landfill sites as well as the substantial involvement of other named third parties with these landfill sites. However, due to the inherent uncertainties of such proceedings, the Company cannot predict the ultimate outcome of these matters. A future change in circumstances with respect to these specific matters or with respect to sites formerly or currently owned or operated by the Company, or with respect to off-site disposal locations used by the Company, could result in future costs to the Company and such amounts could be material. Expenditures during 2008 and the first quarter of 2009 were not material for compliance with environmental control provisions and regulations.

Like other companies in recent years, the Company has been named as a defendant in numerous multi-claimant/multi-defendant lawsuits alleging personal injury as a result of exposure to asbestos, manufactured by third parties, and integrated into or sold with a very limited number of the Company's products. The Company is vigorously defending itself against these claims. Although it is not possible to predict the ultimate outcome of these matters, the Company does not believe the ultimate resolution of these issues will have a material adverse effect on the Company's financial position or results of operations, either from a cash flow perspective or on the financial statements as a whole. This belief is based in part on the fact that no claimant has demonstrated

Table of Contents

exposure to products manufactured or sold by the Company and that a number of cases have been voluntarily dismissed.

See the Special Note Regarding Forward Looking Statements at the front of this Quarterly Report on Form 10-Q and Part I, Item 1A Risk Factors in the Company's Annual Report on Form 10-K for the year ended December 31, 2008 for a discussion of risks and uncertainties that could impact the Company's financial performance and results of operations.

Off-Balance Sheet Arrangements and Contractual Obligations

The Company's off-balance sheet arrangements and contractual obligations are discussed in Part II, Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations under the headings Off-Balance Sheet Arrangements and Contractual Obligations in the Company's Annual Report on Form 10-K for the year ended December 31, 2008, and have not materially changed since that report was filed.

Item 3 Quantitative and Qualitative Disclosures about Market Risk

The Company's quantitative and qualitative disclosures about market risk are included in Part II, Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations under the heading Market Risks in the Company's Annual Report on Form 10-K for the year ended December 31, 2008, and have not materially changed since that report was filed.

Item 4 Controls and Procedures

Evaluation of Disclosure Controls and Procedures

In accordance with Rule 13a-15(b) of the Securities Exchange Act of 1934 (the Exchange Act), the Company's management evaluated, with the participation of the Company's Chairman, President and Chief Executive Officer and the Company's Senior Vice President - Finance, Chief Financial Officer and Treasurer, the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) as of the end of the quarter ended March 31, 2009. Based upon their evaluation of these disclosure controls and procedures, the Company's Chairman, President and Chief Executive Officer and the Company's Senior Vice President - Finance, Chief Financial Officer and Treasurer concluded that the Company's disclosure controls and procedures were effective as of the end of the quarter ended March 31, 2009, to ensure that information relating to the Company, including its consolidated subsidiaries, was made known to management by others within those entities as appropriate to allow timely decisions regarding required disclosure of the information, particularly during the period in which this Quarterly Report on Form 10-Q was being prepared.

Changes in Internal Control over Financial Reporting

There was no change in the Company's internal control over financial reporting that occurred during the quarter ended March 31, 2009, that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Part II Other Information

Item 6 Exhibits

Exhibit No. Description

- 31.1 Certification by the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification by the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32 Certification of Periodic Financial Report by the Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Table of Contents