PEABODY ENERGY CORP
Form 10-Q
May 04, 2012
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

(X)	QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
	For the quarterly period ended March 31, 2012
or	
( )	TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
	For the transition period from ____________ to ____________

Commission File Number: 1-16463

PEABODY ENERGY CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	13-4004153
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
701 Market Street, St. Louis, Missouri	63101-1826
(Address of principal executive offices)	(Zip Code)

(314) 342-3400
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes (X) No ( )

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

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

Large accelerated filer (X)	Accelerated filer ( )	Non-accelerated filer ( )	Smaller reporting company ( )
		(Do not check if a 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 (X)

There were 272,392,200 shares of common stock with a par value of $0.01 per share outstanding at April 27, 2012.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements.

PEABODY ENERGY CORPORATION
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF INCOME

	Three Months Ended March 31,	
	2012	2011
	(Dollars in millions, except per share data)	
Revenues		
Sales	$1,803.0	$1,612.0
Other revenues	235.6	131.1
Total revenues	2,038.6	1,743.1
Costs and expenses		
Operating costs and expenses	1,438.6	1,247.2
Depreciation, depletion and amortization	144.9	107.7
Asset retirement obligation expense	15.2	13.3
Selling and administrative expenses	71.0	61.6
Other operating (income) loss:		
Net gain on disposal or exchange of assets	(4.0)	(4.0)
Loss from equity affiliates	22.7	3.0
Operating profit	350.2	314.3
Interest expense	102.0	51.0
Interest income	(8.1)	(4.1)
Income from continuing operations before income taxes	256.3	267.4
Income tax provision	74.0	72.8
Income from continuing operations, net of income taxes	182.3	194.6
Loss from discontinued operations, net of income taxes	(4.0)	(15.9)
Net income	178.3	178.7
Less: Net income attributable to noncontrolling interests	5.6	2.2
Net income attributable to common stockholders	$172.7	$176.5
Income From Continuing Operations		
Basic earnings per share	$0.64	$0.71
Diluted earnings per share	$0.64	$0.70
Net Income Attributable to Common Stockholders		
Basic earnings per share	$0.63	$0.66
Diluted earnings per share	$0.63	$0.65
Dividends declared per share	$0.085	$0.085

See accompanying notes to unaudited condensed consolidated financial statements.

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PEABODY ENERGY CORPORATION
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Three Months Ended March 31,	
	2012	2011
	(Dollars in millions)	
Net income	$ 178.3	$ 178.7
Other comprehensive income, net of income taxes:		
Net unrealized holding gains (losses) on available-for-sale securities (net of $6.7 and $0.0 tax benefit for the three months ended March 31, 2012 and 2011, respectively)	(11.5)	1.0
Net unrealized gains on cash flow hedges (net of $31.4 and $34.3 tax provision for the three months ended March 31, 2012 and 2011, respectively)		
Increase in fair value of cash flow hedges	147.8	88.5
Less: Reclassification for realized gains included in net income	(84.2)	(56.0)
Net unrealized gains on cash flow hedges	63.6	32.5
Postretirement plans and workers' compensation obligations (net of $8.1 and $0.2 tax provision for the three months ended March 31, 2012 and 2011, respectively)		
Net actuarial loss for the period	—	3.5
Amortization of actuarial loss and prior service cost	13.9	10.0
Postretirement plan and workers' compensation obligations	13.9	13.5
Foreign currency translation adjustment	12.7	—
Other comprehensive income	78.7	47.0
Comprehensive income	257.0	225.7
Less: Comprehensive income attributable to noncontrolling interests	5.6	2.2
Comprehensive income attributable to common stockholders	$ 251.4	$ 223.5

See accompanying notes to unaudited condensed consolidated financial statements.

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PEABODY ENERGY CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS

	(Unaudited) March 31, 2012	December 31, 2011
	(Amounts in millions, except per share data)	
ASSETS		
Current assets		
Cash and cash equivalents	$952.4	$799.1
Accounts receivable, net of allowance for doubtful accounts of $16.6 at March 31, 2012 and $17.0 at December 31, 2011	748.1	922.5
Inventories	514.9	446.3
Assets from coal trading activities, net	43.3	44.6
Deferred income taxes	24.3	27.3
Other current assets	746.7	766.1
Total current assets	3,029.7	3,005.9
Property, plant, equipment and mine development		
Land and coal interests	11,542.1	10,781.0
Buildings and improvements	1,229.8	1,131.4
Machinery and equipment	2,743.0	2,862.4
Less: accumulated depreciation, depletion and amortization	(3,545.8)	(3,412.1)
Property, plant, equipment and mine development, net	11,969.1	11,362.7
Investments and other assets	1,938.3	2,364.4
Total assets	$16,937.1	$16,733.0
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Current maturities of long-term debt	$114.6	$101.1
Liabilities from coal trading activities, net	14.6	10.3
Accounts payable and accrued expenses	1,502.8	1,712.3
Total current liabilities	1,632.0	1,823.7
Long-term debt, less current maturities	6,538.4	6,556.4
Deferred income taxes	590.8	554.2
Asset retirement obligations	637.0	621.3
Accrued postretirement benefit costs	1,051.6	1,053.1
Other noncurrent liabilities	674.5	608.5
Total liabilities	11,124.3	11,217.2
Stockholders' equity		
Preferred Stock — $0.01 per share par value; 10.0 shares authorized, no shares issued or outstanding as of March 31, 2012 or December 31, 2011	—	—
Series A Junior Participating Preferred Stock — $0.01 per share par value; 1.5 shares authorized, no shares issued or outstanding as of March 31, 2012 or December 31, 2011	—	—
Perpetual Preferred Stock — 0.8 shares authorized, no shares issued or outstanding	—	—

as of March 31, 2012 or December 31, 2011		
Series Common Stock — $0.01 per share par value; 40.0 shares authorized, no shares issued or outstanding as of March 31, 2012 or December 31, 2011	—	—
Common Stock — $0.01 per share par value; 800.0 shares authorized, 281.7 shares issued and 272.3 shares outstanding as of March 31, 2012 and 280.3 shares issued and 271.1 shares outstanding as of December 31, 2011	2.8	2.8
Additional paid-in capital	2,255.2	2,234.0
Retained earnings	3,893.5	3,744.0
Accumulated other comprehensive loss	(63.7)	(142.4)
Treasury shares, at cost: 9.4 shares as of March 31, 2012 and 9.2 shares as of December 31, 2011	(361.2)	(353.3)
Peabody Energy Corporation's stockholders' equity	5,726.6	5,485.1
Noncontrolling interests	86.2	30.7
Total stockholders' equity	5,812.8	5,515.8
Total liabilities and stockholders' equity	$16,937.1	$16,733.0

See accompanying notes to unaudited condensed consolidated financial statements.

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PEABODY ENERGY CORPORATION
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three Months Ended March 31, 2012	2011
	(Dollars in millions)	
Cash Flows From Operating Activities		
Net income	$178.3	$178.7
Loss from discontinued operations, net of income taxes	4.0	15.9
Income from continuing operations, net of income taxes	182.3	194.6
Adjustments to reconcile income from continuing operations, net of income taxes to net cash provided by operating activities:		
Depreciation, depletion and amortization	144.9	107.7
Deferred income taxes	0.3	23.9
Share-based compensation	13.0	10.9
Net gain on disposal or exchange of assets	(4.0)	(4.0)
Loss from equity affiliates	22.7	3.0
Changes in current assets and liabilities:		
Accounts receivable	261.6	81.8
Change in receivable from accounts receivable securitization program	(75.0)	—
Inventories	(78.8)	(18.2)
Net assets from coal trading activities	31.6	(72.8)
Other current assets	6.2	(9.2)
Accounts payable and accrued expenses	(108.7)	(102.7)
Asset retirement obligations	13.4	7.3
Workers’ compensation obligations	1.8	7.1
Pension costs	12.4	4.0
Accrued postretirement benefit costs	7.3	6.3
Contributions to pension plans	(0.4)	(0.4)
Other, net	0.8	(4.1)
Net cash provided by continuing operations	431.4	235.2
Net cash used in discontinued operations	(35.9)	(14.6)
Net cash provided by operating activities	395.5	220.6
Cash Flows From Investing Activities		
Additions to property, plant, equipment and mine development	(235.3)	(93.6)
Investment in Prairie State Energy Campus	(3.3)	(8.9)
Proceeds from disposal of assets	4.6	5.5
Investments in equity affiliates and joint ventures	—	(1.1)
Proceeds from sales and maturities of debt and equity securities	3.1	15.5
Purchases of debt and equity securities	—	(14.6)
Purchases of short-term investments	—	(100.0)
Contributions to joint ventures	(208.9)	—
Distributions from joint ventures	221.4	—
Repayment of loans from related parties	338.7	—
Advances to related parties	(322.0)	—
Other, net	(0.5)	(0.4)
Net cash used in continuing operations	(202.2)	(197.6)
Net cash used in discontinued operations	(0.9)	(13.6)
Net cash used in investing activities	(203.1)	(211.2)

Cash Flows From Financing Activities		
Payments of long-term debt	(13.4)	(10.0)
Dividends paid	(23.2)	(23.0)
Repurchase of employee common stock relinquished for tax withholding	(7.9)	(15.1)
Excess tax benefits related to share-based compensation	3.5	4.9
Proceeds from stock options exercised	1.4	4.0
Other, net	0.5	7.8
Net cash used in financing activities	(39.1)	(31.4)
Net change in cash and cash equivalents	153.3	(22.0)
Cash and cash equivalents at beginning of period	799.1	1,295.2
Cash and cash equivalents at end of period	$952.4	$1,273.2

See accompanying notes to unaudited condensed consolidated financial statements.

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PEABODY ENERGY CORPORATION
UNAUDITED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

	Peabody Energy Corporation's Stockholders' Equity						
	Common Stock	Additional Paid-in Capital	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Noncontrolling Interests	Total Stockholders' Equity
	(Dollars in millions)						
December 31, 2011	$2.8	$2,234.0	$(353.3)	$3,744.0	$ (142.4)	$ 30.7	$ 5,515.8
Net income	—	—	—	172.7	—	5.6	178.3
Net unrealized losses on available-for-sale securities (net of $6.7 tax benefit)	—	—	—	—	(11.5)	—	(11.5)
Increase in fair value of cash flow hedges (net of $31.4 tax provision)	—	—	—	—	63.6	—	63.6
Postretirement plans and workers' compensation obligations (net of $8.1 tax provision)	—	—	—	—	13.9	—	13.9
Foreign currency translation adjustment	—	—	—	—	12.7	—	12.7
Dividends paid	—	—	—	(23.2)	—	—	(23.2)
Share-based compensation	—	13.0	—	—	—	—	13.0
Excess tax benefits related to share-based compensation	—	3.5	—	—	—	—	3.5
Stock options exercised	—	1.4	—	—	—	—	1.4
Employee stock purchases	—	3.3	—	—	—	—	3.3
Repurchase of employee common stock relinquished for tax withholding	—	—	(7.9)	—	—	—	(7.9)
MCG Coal Holdings Pty Ltd. noncontrolling interests at conversion	—	—	—	—	—	53.4	53.4
Distributions to noncontrolling interests	—	—	—	—	—	(3.5)	(3.5)
March 31, 2012	$2.8	$2,255.2	$(361.2)	$3,893.5	$ (63.7)	$ 86.2	$ 5,812.8

See accompanying notes to unaudited condensed consolidated financial statements.

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PEABODY ENERGY CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(1) Basis of Presentation
The condensed consolidated financial statements include the accounts of Peabody Energy Corporation (the Company) and its affiliates. All intercompany transactions, profits and balances have been eliminated in consolidation.
The accompanying condensed consolidated financial statements as of March 31, 2012 and for the three months ended March 31, 2012 and 2011, and the notes thereto, are unaudited. However, in the opinion of management, these financial statements reflect all normal, recurring adjustments necessary for a fair presentation of the results of the periods presented. The balance sheet information as of December 31, 2011 has been derived from the Company’s audited consolidated balance sheet. The results of operations for the three months ended March 31, 2012 are not necessarily indicative of the results to be expected for future quarters or for the year ending December 31, 2012.
The Company classifies items within discontinued operations in the unaudited condensed consolidated financial statements when the operations and cash flows of a particular component (defined as operations and cash flows that can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity) of the Company have been (or will be) eliminated from the ongoing operations of the Company as a result of a disposal transaction, and the Company will no longer have any significant continuing involvement in the operations of that component.
(2) Newly Adopted Accounting Standards and Accounting Standards Not Yet Implemented
In January 2010, the Financial Accounting Standards Board (FASB) issued accounting guidance that required new fair value disclosures, including disclosures about significant transfers into and out of Level 1 and Level 2 fair value measurements and a description of the reasons for the transfers. In addition, the guidance required new disclosures regarding activity in Level 3 fair value measurements, including a gross basis reconciliation. The Company began complying with the new fair value disclosure requirements beginning January 1, 2010, except for the disclosure of activity within Level 3 fair value measurements, which became effective January 1, 2011. In May 2011, the FASB issued additional fair value measurement disclosure requirements that were intended to provide a consistent definition of fair value and ensure that the fair value measurement and disclosure requirements are similar between United States (U.S.) generally accepted accounting principles (GAAP) and International Financial Reporting Standards. That update required the categorization by level for financial instruments not measured at fair value but for which disclosure of fair value is required, disclosure of all transfers between Level 1 and Level 2, and additional disclosures for Level 3 measurements regarding the sensitivity of fair value to changes in unobservable inputs and any interrelationships between those inputs. The guidance became effective for interim and annual periods beginning after December 15, 2011 (January 1, 2012 for the Company). While the adoption of this guidance had an impact on the Company's disclosures, it did not affect the Company's results of operations, financial condition or cash flows.
(3) Acquisition of Macarthur Coal Limited
On October 23, 2011, PEAMCoal Pty Ltd (PEAMCoal), an Australian company that was then indirectly owned 60% by the Company and 40% by ArcelorMittal, acquired a majority interest in Macarthur Coal Limited (Macarthur) through an all cash off-market takeover offer. On October 26, 2011 (the acquisition and control date), the Company appointed its nominees to the Macarthur Board of Directors and executive management team. The acquisition was completed on December 20, 2011 as PEAMCoal acquired all of Macarthur's remaining outstanding shares of common stock for $4.8 billion, net of $261.2 million of acquired cash, of which the Company's share was $2.8 billion. PEAMCoal accounted for share acceptances under the takeover process as a single transaction occurring on October 26, 2011. On December 21, 2011, the Company acquired ArcelorMittal Mining Australasia B.V., an indirect subsidiary of ArcelorMittal that indirectly owned 40% of PEAMCoal, for $2.0 billion resulting in the Company's 100% ownership of Macarthur.

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The preliminary purchase accounting allocations were recorded in the accompanying unaudited condensed consolidated financial statements as of, and for the periods subsequent to the acquisition and control date. The Company has not yet finalized the fair value determination of the assets acquired and liabilities assumed, which is expected once third-party valuation appraisals are completed. The Company is evaluating mine lives and reviewing coal reserve studies on the acquired properties, the outcome of which will determine the final fair value allocated to coal reserve assets. The following table summarizes the preliminary estimated fair values of assets acquired and liabilities assumed that were recognized at the acquisition and control date as well as provisional fair value adjustments made during the first quarter of 2012:

	Preliminary Allocations	Adjustments	Updated Allocations
	(Dollars in millions)		
Accounts receivable, net	$106.6	$7.7	$114.3
Inventories	67.1	(10.1)	57.0
Other current assets	137.5	(3.9)	133.6
Property, plant, equipment and mine development	3,457.0	112.5	3,569.5
Investments and other assets	1,275.1	(78.7)	1,196.4
Current maturities of long-term debt	(11.0)	—	(11.0)
Accounts payable and accrued expenses	(133.8)	(25.0)	(158.8)
Long-term debt, less current maturities	(59.2)	—	(59.2)
Asset retirement obligations	(39.3)	—	(39.3)
Other noncurrent liabilities	(31.4)	(2.5)	(33.9)
Noncontrolling interests	(2,011.9)	—	(2,011.9)
Total purchase price, net of cash acquired of $261.2	$2,756.7	$—	$2,756.7

The adjustments to the provisional fair values result from additional information obtained about facts in existence at the acquisition and control date. Adjustments to provisional fair values are assumed to have been made as of the acquisition and control date. As a result, "Operating costs and expenses" and "Depreciation, depletion and amortization" for the fourth quarter of 2011 would have been lower by $10.1 million and $10.6 million, respectively, than was previously reported. The results in the unaudited condensed consolidated statements of income reflect these adjustments in the first quarter of 2012.

In connection with the acquisition, the Company acquired contract based intangibles consisting of port, rail and water take-or-pay obligations and recorded a liability for unutilized capacity of $33.3 million, net of tax, which is being amortized based on that unutilized capacity over the terms of the applicable agreements which extend to 2018. As of March 31, 2012, the carrying value of the liability was $30.2 million and the amortization (reduction to “Operating costs and expenses” in the unaudited condensed consolidated statement of income) recorded through March 31, 2012 was $3.1 million. Estimated amortization as of March 31, 2012 is $11.4 million, $17.1 million and $1.7 million for the years ending December 31, 2012, 2013 and 2014, respectively. Unutilized capacity is not expected in years 2015 through 2018.

Macarthur contributed revenues of $145.2 million and a net loss of $6.5 million during the three months ended March 31, 2012, which includes results from our equity affiliate investment in the Middlemount Mine which is ramping up operations. The results of Macarthur for the three months ended March 31, 2012 are included in the unaudited condensed consolidated statements of income and are reported in the Australian Mining segment, except for the activity associated with certain equity affiliate investments, which is reflected in the Corporate and Other segment.

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The following unaudited pro forma financial information presents the combined results of operations of the Company and Macarthur, on a pro forma basis, as though the companies had been combined as of January 1, 2011. The unaudited pro forma financial information does not necessarily reflect the results of operations that would have occurred had the Company and Macarthur constituted a single entity during those periods or that may be attained in the future.

	Three Months Ended March 31, 2011 (Dollars in millions, except earnings per share)
Revenue	$1,807.8
Income from continuing operations, net of income taxes	113.1
Basic earnings per share	0.35
Diluted earnings per share	0.35

The pro forma income from continuing operations, net of income taxes, includes adjustments to operating costs to reflect the additional expense for the estimated impact of the fair value adjustment for coal inventory, the estimated impact on depreciation, depletion and amortization for the fair value adjustment for property, plant and equipment (including mineral rights) and additional expense for the estimated impact of reflecting the equity affiliate interest at its estimated fair value.

As disclosed in Note 23 to the Consolidated Financial Statements in the Company’s Annual Report on Form 10-K for the year ended December 31, 2011, an outstanding loan balance of $384.6 million was converted to a 90% equity interest in MCG Coal Holdings Pty Ltd. (MCGH), resulting in consolidation of MCGH and recognition of noncontrolling interests of $53.4 million at conversion.

(4) Discontinued Operations

Discontinued operations include certain non-strategic Midwestern and Australian mining assets held for sale where the Company has committed to the divestiture of such assets and other operations recently divested.

Revenues resulting from discontinued operations (including assets held for sale) were $48.4 million and $1.8 million for the three months ended March 31, 2012 and March 31, 2011, respectively. Losses before income taxes from discontinued operations were $8.2 million and $21.5 million for the three months ended March 31, 2012 and March 31, 2011, respectively. The income tax adjustment resulting from discontinued operations reflects a benefit of $4.2 million and $5.6 million for the three months ended March 31, 2012 and March 31, 2011, respectively.

Total assets related to discontinued operations were $156.3 million as of March 31, 2012 and $143.7 million as of December 31, 2011. Total liabilities associated with discontinued operations were $65.9 million as of March 31, 2012 and $86.3 million as of December 31, 2011.

(5) Investments

The Company’s short-term investments are defined as those investments with original maturities of greater than three months and up to one year, and long-term investments are defined as those investments with original maturities greater than one year.

The Company classifies its investments as either held-to-maturity or available-for-sale at the time of purchase and reevaluates such designation periodically. Investments are classified as held-to-maturity when the Company has the intent and ability to hold the securities to maturity.

Investments in securities not classified as held-to-maturity are classified as available-for-sale. Available-for-sale securities are carried at fair value, with unrealized gains and losses, net of income taxes, reported in “Accumulated other comprehensive loss” in the condensed consolidated balance sheets. Realized gains and losses, determined on a specific identification method, are included in “Interest income” in the unaudited condensed consolidated statements of income.

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PEABODY ENERGY CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Continued)

The Company did not have any held-to-maturity securities as of March 31, 2012 or December 31, 2011.
Investments in available-for-sale securities at March 31, 2012 were as follows:

Available-for-sale securities	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in millions)			
Current:				
Federal government securities	$2.9	$—	$—	$2.9
U.S. corporate bonds	5.2	—	—	5.2
Noncurrent:				
Marketable equity securities	66.5	—	(27.6)	38.9
Federal government securities	11.3	0.2	—	11.5
U.S. corporate bonds	4.9	0.2	—	5.1
Total	$90.8	$0.4	$(27.6)	$63.6

Investments in available-for-sale securities at December 31, 2011 were as follows:

Available-for-sale securities	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
		(Dollars in millions)		
Current:				
Federal government securities	$3.3	$—	$—	$3.3
U.S. corporate bonds	3.9	—	—	3.9
Noncurrent:				
Marketable equity securities	66.5	—	(9.5)	57.0
Federal government securities	11.3	0.2	—	11.5
U.S. corporate bonds	7.7	0.1	—	7.8
Total	$92.7	$0.3	$(9.5)	$83.5

Contractual maturities for available-for-sale investments in debt securities at March 31, 2012 were as shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Contractual maturities for available-for-sale securities	Cost	Fair Value
	(Dollars in millions)	
Due in one year or less	$8.1	$8.1
Due in one to five years	16.2	16.6
Total	$24.3	$24.7

The Company’s investments in marketable equity securities consist of an investment in Winsway Coking Coal Holdings Limited.
Proceeds from sales and maturities of securities amounted to $1.7 million with no realized gain or loss on the sales for the three months ended March 31, 2012.

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In addition to the securities described above, the Company held investments in debt securities related to the Company's pro-rata share of funding in the Newcastle Coal Infrastructure Group (NCIG). These debt securities are recorded at cost, which approximates fair value, and are denominated in U.S. dollars. During the three months ended March 31, 2012, the Company sold $1.4 million of the debt securities related to NCIG, with no realized gain or loss on the sale. The fair value of these securities still held at March 31, 2012 was $28.0 million.

At each reporting date, the Company performs separate evaluations of debt and equity securities to determine if any unrealized losses are other-than-temporary. None of the securities that were in an unrealized loss position at March 31, 2012 has been so for greater than 12 months. The Company did not recognize any other-than-temporary losses on any of its investments during the three months ended March 31, 2012.

(6) Inventories

Inventories consisted of the following:

	March 31, 2012	December 31, 2011
	(Dollars in millions)	
Materials and supplies	$134.6	$124.9
Raw coal	125.1	95.0
Saleable coal	255.2	226.4
Total	$514.9	$446.3

(7) Derivatives and Fair Value Measurements

Risk Management — Non-Coal Trading Activities

The Company is exposed to various types of risk in the normal course of business, including price risk on commodities utilized in the Company's operations, interest rate risk on long-term debt, and foreign currency exchange rate risk for non-U.S. dollar expenditures. In most cases, commodity price risk (excluding coal trading activities) related to the sale of coal is mitigated through the use of long-term, fixed-price contracts, with a small percentage mitigated through the use of financial instruments. For the price risk exposure on other commodities, as well as for the interest rate risk and foreign currency exchange rate risk, the Company utilizes financial derivative instruments to manage the risks related to these fluctuations. All of these risks are actively monitored in an effort to ensure compliance with the risk management policies of the Company.

Interest Rate Swaps. The Company is exposed to interest rate risk on its fixed rate and variable rate long-term debt. From time to time, the Company manages the interest rate risk associated with the fair value of its fixed rate borrowings using fixed-to-floating interest rate swaps to effectively convert a portion of the underlying cash flows on the debt into variable rate cash flows. The Company designates these swaps as fair value hedges, with the objective of hedging against changes in the fair value of the fixed rate debt that results from market interest rate changes. From time to time, the interest rate risk associated with the Company’s variable rate borrowings is managed using floating-to-fixed interest rate swaps. The Company designates these swaps as cash flow hedges, with the objective of reducing the variability of cash flows associated with market interest rate changes. As of March 31, 2012, the Company had no interest rate swaps in place.

Foreign Currency Hedges. The Company is exposed to foreign currency exchange rate risk, primarily on Australian dollar expenditures made in its Australian Mining segment. This risk is managed by entering into forward contracts and options that the Company designates as cash flow hedges, with the objective of reducing the variability of cash flows associated with forecasted foreign currency expenditures.

Diesel Fuel and Explosives Hedges. The Company is exposed to commodity price risk associated with diesel fuel and explosives in the U.S. and Australia. This risk is managed through the use of cost pass-through contracts and derivatives, primarily swaps. The Company generally designates the swap contracts as cash flow hedges, with the objective of reducing the variability of cash flows associated with forecasted diesel fuel and explosives purchases.

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Notional Amounts and Fair Value. The following summarizes the Company’s foreign currency and commodity positions at March 31, 2012:

	Notional Amount by Year of Maturity						
	Total	2012	2013	2014	2015	2016	2017 and thereafter
Foreign Currency							
A$:US$ hedge contracts (A$ millions)	$4,565.5	$1,694.9	$1,651.6	$1,117.5	$101.5	$—	$—
GBP:US$ hedge contracts (GBP millions)	6.5	6.5	—	—	—	—	—
Commodity Contracts							
Diesel fuel hedge contracts (million gallons)	190.0	72.3	73.7	41.0	3.0	—	—
U.S. explosives hedge contracts (million MMBtu)	6.6	2.8	2.6	1.2	—	—	—

	Account Classification by			
	Cash Flow Hedge	Fair Value Hedge	Economic Hedge	Fair Value Asset (Liability) (Dollars in millions)
Foreign Currency				
A$:US$ hedge contracts (A$ millions)	$4,565.5	$—	$—	$517.9
GBP:US$ hedge contracts (GBP millions)	6.5	—	—	—
Commodity Contracts				
Diesel fuel hedge contracts (million gallons)	190.0	—	—	81.9
U.S. explosives hedge contracts (million MMBtu)	6.6	—	—	(12.7)

Hedge Ineffectiveness. The Company assesses, both at inception and at least quarterly thereafter, whether the derivatives used in hedging activities are highly effective at offsetting the changes in the anticipated cash flows of the hedged item. The effective portion of the change in the fair value is recorded in “Accumulated other comprehensive loss” until the hedged transaction impacts reported earnings, at which time any gain or loss is also reclassified to earnings. To the extent that the periodic changes in the fair value of the derivatives exceed the changes in the hedged item, the ineffective portion of the periodic non-cash changes are recorded in earnings in the period of the change. If the hedge ceases to qualify for hedge accounting, the Company prospectively recognizes the mark-to-market movements in earnings in the period of the change.

A measure of ineffectiveness is inherent in hedging future diesel fuel purchases with derivative positions based on crude oil and refined petroleum products as a result of location and product differences.

The Company’s derivative positions for the hedging of future explosives purchases are based on natural gas, which is the primary price component of explosives. However, a small measure of ineffectiveness exists as the contractual purchase price includes manufacturing fees that are subject to periodic adjustments. In addition, other fees, such as transportation surcharges, can result in ineffectiveness, but have historically changed infrequently and comprise a small portion of the total explosives cost.

The Company’s derivative positions for the hedging of forecasted foreign currency expenditures contain a small measure of ineffectiveness due to timing differences between the hedge settlement and the purchase transaction, which could differ by less than a day and up to a maximum of 30 days.

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The tables below show the classification and amounts of pre-tax gains and losses related to the Company's non-trading hedges during the three months ended March 31, 2012 and 2011:

		Three Months Ended March 31, 2012			
Financial Instrument	Income Statement Classification Gains (Losses) - Realized	Gain recognized in income on non-designated derivatives	Gain recognized in other comprehensive income on derivative (effective portion)	Gain reclassified from other comprehensive income into income (effective portion)	Gain reclassified from other comprehensive income into income (ineffective portion)
		(Dollars in millions)			
Commodity swaps and options	Operating costs and expenses	$—	$ 58.1	$ 17.3	$ 4.6
Foreign currency cash flow hedge contracts:	Operating costs and expenses	—	140.3	113.0	—
Total		$—	$ 198.4	$ 130.3	$ 4.6

		Three Months Ended March 31, 2011			
Financial Instrument	Income Statement Classification Gains (Losses) - Realized	Gain recognized in income on non-designated derivatives	Gain recognized in other comprehensive income on derivative (effective portion)	Gain reclassified from other comprehensive income into income (effective portion)	Gain reclassified from other comprehensive income into income (ineffective portion)
		(Dollars in millions)			
Commodity swaps and options	Operating costs and expenses	$—	$ 99.0	$ 8.1	$ 2.3
Foreign currency cash flow hedge contracts	Operating costs and expenses	—	119.8	72.7	—
Total		$—	$ 218.8	$ 80.8	$ 2.3

Based on the net fair value of the Company's non-coal trading positions held in "Accumulated other comprehensive loss" at March 31, 2012, unrealized gains to be reclassified from comprehensive income to earnings over the next 12 months associated with the Company's foreign currency and diesel fuel hedge programs are expected to be approximately $284 million and $61 million, respectively, while the unrealized losses to be realized under the explosives hedge program are expected to be approximately $8 million. As these unrealized gains are associated with derivative instruments that represent hedges of forecasted transactions, the amounts reclassified to earnings will partially offset the realized transactions, while the unrealized losses will add incremental expense to the unaudited condensed consolidated statements of income.

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The classification and amount of derivatives presented on a gross basis as of March 31, 2012 and December 31, 2011 are as follows:

Financial Instrument	Fair Value as of March 31, 2012			
	Current Assets	Noncurrent Assets	Current Liabilities	Noncurrent Liabilities
	(Dollars in millions)			
Commodity swaps and options	$61.2	$22.2	$8.2	$6.0
Foreign currency cash flow hedge contracts	284.8	235.6	1.7	0.8
Total	$346.0	$257.8	$9.9	$6.8

Financial Instrument	Fair Value as of December 31, 2011			
	Current Assets	Noncurrent Assets	Current Liabilities	Noncurrent Liabilities
	(Dollars in millions)			
Commodity swaps and options	$43.4	$11.7	$7.1	$15.0
Foreign currency cash flow hedge contracts	270.4	229.0	4.3	4.5
Total	$313.8	$240.7	$11.4	$19.5

After netting by counterparty where permitted, the fair values of the respective derivatives are reflected in “Other current assets,” “Investments and other assets,” “Accounts payable and accrued expenses” and “Other noncurrent liabilities” in the condensed consolidated balance sheets.

See Note 8 for information related to the Company’s coal trading activities.

Fair Value Measurements

The Company uses a three-level fair value hierarchy that categorizes assets and liabilities measured at fair value based on the observability of the inputs utilized in the valuation. These levels include: Level 1, inputs are quoted prices in active markets for the identical assets or liabilities; Level 2, inputs other than quoted prices included in Level 1 that are directly or indirectly observable through market-corroborated inputs; and Level 3, inputs are unobservable, or observable but cannot be market-corroborated, requiring the Company to make assumptions about pricing by market participants.

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Financial Instruments Measured on a Recurring Basis. The following tables set forth the hierarchy of the Company's net financial asset positions for which fair value is measured on a recurring basis:

	March 31, 2012			
	Level 1	Level 2	Level 3	Total
	(Dollars in millions)			
Investment in debt and equity securities	$63.6	$—	$—	$63.6
Commodity swaps and options	—	69.2	—	69.2
Foreign currency cash flow hedge contracts	—	517.9	—	517.9
Total net financial assets	$63.6	$587.1	$—	$650.7

	December 31, 2011			
	Level 1	Level 2	Level 3	Total
	(Dollars in millions)			
Investment in debt and equity securities	$83.5	$—	$—	$83.5
Commodity swaps and options	—	33.0	—	33.0
Foreign currency cash flow hedge contracts	—	490.6	—	490.6
Total net financial assets	$83.5	$523.6	$—	$607.1

For Level 1 and 2 financial assets and liabilities, the Company utilizes both direct and indirect observable price quotes, including interest rate yield curves, exchange indices, broker quotes, published indices and other market quotes. Below is a summary of the Company's valuation techniques for Level 1 and 2 financial assets and liabilities:

- Investment in debt and equity securities: valued based on quoted prices in active markets (Level 1).
- Commodity swaps and options — diesel fuel and explosives: generally valued based on a valuation that is corroborated by the use of market-based pricing (Level 2).
- Foreign currency cash flow hedge contracts: valued utilizing inputs obtained in quoted public markets (Level 2).

The Company did not have any transfers between levels during the three months ended March 31, 2012 or 2011 for its non-coal trading positions. The Company's policy is to value all transfers between levels using the beginning of period valuation.

Other Financial Instruments. The following methods and assumptions were used by the Company in estimating fair values for other financial instruments as of March 31, 2012 and December 31, 2011:

- Cash and cash equivalents, accounts receivable, including those within the Company's accounts receivable securitization program, and accounts payable and accrued expenses have carrying values which approximate fair value due to the short maturity or the liquid nature of these instruments.
- The Company's investments in debt and equity securities related to the Company's pro-rata share of funding in NCIG are included in "Investments and other assets" in the condensed consolidated balance sheets. The debt securities are recorded at cost, which approximates fair value.
- Long-term debt fair value estimates are based on observed prices for securities with an active trading market when available (Level 2), and otherwise on estimated borrowing rates to discount the cash flows to their present value (Level 3). The carrying amounts of the 7.875% Senior Notes due 2026 and the Convertible Junior Subordinated Debentures due 2066 (the Debentures) are net of the respective unamortized note discounts.

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The carrying amounts and estimated fair values of the Company's debt are summarized as follows:

	March 31, 2012		December 31, 2011	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(Dollars in millions)			
Long-term debt	$6,653.0	$6,622.3	$6,657.5	$6,922.7

Nonperformance and Credit Risk

The fair value of the Company's non-coal trading derivative assets and liabilities reflects adjustments for nonperformance and credit risk. The Company manages its counterparty risk through established credit standards, diversification of counterparties, utilizing investment grade commercial banks and continuous monitoring of counterparty creditworthiness. To reduce its credit exposure for these hedging activities, the Company seeks to enter into netting agreements with counterparties that permit the Company to offset asset and liability positions with such counterparties.

(8) Coal Trading

Risk Management

The Company engages in direct and brokered trading of coal, ocean freight and fuel-related commodities in over-the-counter markets (coal trading), some of which is subsequently exchange-cleared and some of which is bilaterally-settled. Except those for which the Company has elected to apply a normal purchases and normal sales exception, all derivative coal trading contracts are accounted for on a fair value basis.

The Company's policy is to include instruments associated with coal trading transactions as a part of its trading book. Trading revenues are recorded in "Other revenues" in the unaudited condensed consolidated statements of income and include realized and unrealized gains and losses on derivative instruments, including coal deliveries related to contracts accounted for under the normal purchases and normal sales exception. Therefore, the Company has elected the trading exemption to reflect the disclosures for its coal trading activities.

	Three Months Ended March 31,	
Trading Revenues by Type of Instrument	2012	2011
	(Dollars in millions)	
Commodity swaps and options	$10.8	$(31.8)
Physical commodity purchase/sale contracts	9.1	21.9
Total trading revenues	$19.9	$(9.9)

Hedge Ineffectiveness. The Company assesses, both at inception and at least quarterly thereafter, whether the derivatives used in hedging activities are highly effective at offsetting the changes in the anticipated cash flows of the hedged item. The effective portion of the change in the fair value is recorded in "Accumulated other comprehensive loss" until the hedged transaction impacts reported earnings, at which time gains and losses are also reclassified to earnings. To the extent that the periodic changes in the fair value of the derivatives exceed the changes in the hedged item, the ineffective portion of the periodic non-cash changes are recorded in earnings in the period of the change. If the hedge ceases to qualify for hedge accounting, the Company prospectively recognizes the mark-to-market movements in earnings in the period of the change.

In some instances, the Company has designated an existing coal trading derivative as a hedge and, thus, the derivative has a non-zero fair value at hedge inception. The "off-market" nature of these derivatives, which is best described as an embedded financing element within the derivative, is a source of ineffectiveness. In other instances, the Company uses a coal trading derivative that settles at a different time, has different quality specifications, or has a different location basis than the occurrence of the cash flow being hedged. These collectively yield ineffectiveness to the extent that the derivative hedge contract does not exactly offset changes in the fair value or expected cash flows of the hedged item.

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Forecasted Transactions No Longer Probable. During the three months ended March 31, 2012, the Company reclassified losses of $1.2 million out of "Accumulated other comprehensive loss" to earnings as the underlying forecasted transactions were deemed no longer probable of occurring.

Fair Value Measurements

The fair value of assets and liabilities from coal trading activities is set forth below:

	March 31, 2012		December 31, 2011	
	Gross Basis	Net Basis	Gross Basis	Net Basis
	(Dollars in millions)			
Assets from coal trading activities	$196.0	$43.3	$170.4	$44.6
Liabilities from coal trading activities	(95.7)	(14.6)	(84.0)	(10.3)
Subtotal	100.3	28.7	86.4	34.3
Net margin held [(1)]	(71.6)	—	(52.1)	—
Net value of coal trading positions	$28.7	$28.7	$34.3	$34.3

(1) Represents margin held from exchanges of $71.6 million and $52.1 million at March 31, 2012 and December 31, 2011, respectively. Of the margin held at March 31, 2012 and December 31, 2011, approximately $50 million and $23 million, respectively, related to cash flow hedges.

The Company's trading assets and liabilities are generally made up of forward contracts, financial swaps and margin. The fair value of coal trading positions designated as cash flow hedges of forecasted sales was an asset (before application of margin) of $48.8 million and $22.4 million as of March 31, 2012 and December 31, 2011, respectively.

The following tables set forth the hierarchy of the Company's net financial asset (liability) coal trading positions for which fair value is measured on a recurring basis:

	March 31, 2012			
	Level 1	Level 2	Level 3	Total
	(Dollars in millions)			
Commodity swaps and options	$5.0	$11.0	$—	$16.0
Physical commodity purchase/sale contracts	—	3.8	8.9	12.7
Total net financial assets	$5.0	$14.8	$8.9	$28.7

	December 31, 2011			
	Level 1	Level 2	Level 3	Total
	(Dollars in millions)			
Commodity swaps and options	$21.2	$(1.9)	$—	$19.3
Physical commodity purchase/sale contracts	—	6.3		