FULLER H B CO
Form 10-Q
June 27, 2014

**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 May 31, 2014**

**OR**

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

**For the transition period from __________ to __________**

**Commission file number: 001-09225**

**H.B. FULLER COMPANY**

**(Exact name of registrant as specified in its charter)**

| | |
|---|---|
| **Minnesota** | **41-0268370** |
| **(State or other jurisdiction of incorporation or organization)** | **(I.R.S. Employer Identification No.)** |
| **1200 Willow Lake Boulevard, St. Paul, Minnesota** | **55110-5101** |
| **(Address of principal executive offices)** | **(Zip Code)** |

**(651) 236-5900**

**(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 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 ¨ (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 Act). Yes ¨ No x

The number of shares outstanding of the Registrant s Common Stock, par value $1.00 per share, was 50,215,987 as of June 19, 2014.

**PART I. FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**H.B. FULLER COMPANY AND SUBSIDIARIES**

**Condensed Consolidated Statements of Income**

(In thousands, except per share amounts)

(Unaudited)

| | 13 Weeks Ended | | 26 Weeks Ended | |
|---|---|---|---|---|
| | May 31, 2014 | June 1, 2013 | May 31, 2014 | June 1, 2013 |
| **Net revenue** | **$ 544,034** | $ 519,016 | **$ 1,030,015** | $ 998,858 |
| Cost of sales | **(401,379)** | (372,400) | **(754,315)** | (718,866) |
| Gross profit | **142,655** | 146,616 | **275,700** | 279,992 |
| Selling, general and administrative expenses | **(96,372)** | (93,806) | **(193,171)** | (191,446) |
| Special charges, net | **(13,538)** | (10,843) | **(25,272)** | (16,176) |
| Other income (expense), net | **(204)** | (1,814) | **(1,254)** | (1,436) |
| Interest expense | **(4,760)** | (4,884) | **(8,886)** | (10,211) |
| **Income before income taxes and income from equity method investments** | **27,781** | 35,269 | **47,117** | 60,723 |
| Income taxes | **(8,838)** | (10,864) | **(15,379)** | (17,984) |
| Income from equity method investments | **1,683** | 1,643 | **3,537** | 4,083 |
| **Net income including non-controlling interests** | **20,626** | 26,048 | **35,275** | 46,822 |
| Net income attributable to non-controlling interests | **(89)** | (119) | **(167)** | (216) |
| **Net income attributable to H.B. Fuller** | **$ 20,537** | $ 25,929 | **$ 35,108** | $ 46,606 |
| **Earnings per share attributable to H.B. Fuller common stockholders:** | | | | |
| Basic | **$ 0.41** | $ 0.52 | **$ 0.70** | $ 0.93 |
| Diluted | **$ 0.40** | $ 0.51 | **$ 0.69** | $ 0.91 |
| **Weighted-average common shares outstanding:** | | | | |
| Basic | **49,956** | 49,935 | **49,933** | 49,876 |
| Diluted | **51,175** | 51,152 | **51,215** | 51,090 |
| **Dividends declared per common share** | **$ 0.120** | $ 0.100 | **$ 0.220** | $ 0.185 |

See accompanying Notes to Condensed Consolidated Financial Statements.

**H.B. FULLER COMPANY AND SUBSIDIARIES**

**Condensed Consolidated Statements of Comprehensive Income**

(In thousands)

(Unaudited)

| | 13 Weeks Ended | | 26 Weeks Ended | |
|---|---|---|---|---|
| | **May 31, 2014** | **June 1, 2013** | **May 31, 2014** | **June 1, 2013** |
| **Net income including non-controlling interests** | **$ 20,626** | $ 26,048 | **$ 35,275** | $ 46,822 |
| Other comprehensive income (loss) | | | | |
| Foreign currency translation | **(1,377)** | (5,647) | **(830)** | (9,109) |
| Defined benefit pension plans adjustment, net of tax | **1,021** | 1,965 | **2,039** | 3,941 |
| Interest rate swaps, net of tax | **10** | 10 | **20** | 20 |
| Cash-flow hedges, net of tax | **29** | (21) | **32** | 189 |
| **Other comprehensive income (loss)** | **(317)** | (3,693) | **1,261** | (4,959) |
| Comprehensive income | **20,309** | 22,355 | **36,536** | 41,863 |
| Less: Comprehensive income attributable to non-controlling interests | **97** | 73 | **164** | 177 |
| **Comprehensive income attributable to H.B. Fuller** | **$ 20,212** | $ 22,282 | **$ 36,372** | $ 41,686 |

See accompanying Notes to Condensed Consolidated Financial Statements.

**H.B. FULLER COMPANY AND SUBSIDIARIES**

**Condensed Consolidated Balance Sheets**

(In thousands, except share and per share amounts)

(Unaudited)

| | May 31, 2014 | November 30, 2013 |
|---|---|---|
| **Assets** | | |
| **Current assets:** | | |
| Cash and cash equivalents | **$ 95,044** | $ 155,121 |
| Trade receivables (net of allowances $8,951 and $8,539, for May 31, 2014 and November 30, 2013, respectively) | **354,436** | 331,125 |
| Inventories | **281,914** | 221,537 |
| Other current assets | **99,272** | 85,046 |
| Current assets of discontinued operations | **1,865** | 1,865 |
| **Total current assets** | **832,531** | 794,694 |
| Property, plant and equipment | **1,100,261** | 1,032,792 |
| Accumulated depreciation | **(615,213)** | (598,405) |
| **Property, plant and equipment, net** | **485,048** | 434,387 |
| Goodwill | **264,389** | 263,103 |
| Other intangibles, net | **208,200** | 219,401 |
| Other assets | **170,647** | 161,443 |
| **Total assets** | **$ 1,960,815** | $ 1,873,028 |
| **Liabilities, redeemable non-controlling interest and total equity** | | |
| **Current liabilities:** | | |
| Notes payable | **$ 29,466** | $ 20,589 |
| Trade payables | **222,284** | 201,575 |
| Accrued compensation | **51,431** | 76,218 |
| Income taxes payable | **8,233** | 10,830 |
| Other accrued expenses | **52,330** | 46,566 |
| Current liabilities of discontinued operations | **5,000** | 5,000 |
| **Total current liabilities** | **368,744** | 360,778 |
| Long-term debt, excluding current maturities | **536,584** | 472,315 |
| Accrued pension liabilities | **45,988** | 52,922 |
| Other liabilities | **49,755** | 51,835 |
| **Total liabilities** | **1,001,071** | 937,850 |

| | | |
|---|---|---|
| Commitments and contingencies | | |
| **Redeemable non-controlling interest** | **4,886** | 4,717 |
| **Equity:** | | |
| H.B. Fuller stockholders equity: | | |
| Preferred stock (no shares outstanding) Shares authorized 10,045,900 | | |
| Common stock, par value $1.00 per share, Shares authorized 160,000,000, Shares outstanding 50,193,237 and 50,228,543, for May 31, 2014 and November 30, 2013, respectively | **50,193** | 50,229 |
| Additional paid-in capital | **43,647** | 44,490 |
| Retained earnings | **931,311** | 907,308 |
| Accumulated other comprehensive income (loss) | **(70,698)** | (71,962) |
| Total H.B. Fuller stockholders equity | **954,453** | 930,065 |
| Non-controlling interests | **405** | 396 |
| **Total equity** | **954,858** | 930,461 |
| **Total liabilities, redeemable non-controlling interest and total equity** | **$ 1,960,815** | $ 1,873,028 |

See accompanying Notes to Condensed Consolidated Financial Statements.

**H.B. FULLER COMPANY AND SUBSIDIARIES**

**Condensed Consolidated Statements of Total Equity**

(In thousands)

(Unaudited)

| | H.B. Fuller Company Shareholders | | | | | |
|---|---|---|---|---|---|---|
| | **Common Stock** | **Additional Paid-in Capital** | **Retained Earnings** | **Accumulated Other Comprehensive Income (Loss)** | **Non-Controlling Interests** | **Total** |
| **Balance at December 1, 2012** | $ 49,903 | $ 37,965 | $ 830,031 | $ (139,626) | $ 425 | $ 778,698 |
| Comprehensive income | | | 96,761 | 67,664 | 370 | 164,795 |
| Dividends | | | (19,484) | | | (19,484) |
| Stock option exercises | 462 | 8,429 | | | | 8,891 |
| Share-based compensation plans other, net | 301 | 12,621 | | | | 12,922 |
| Excess tax benefit on share-based compensation | | 2,676 | | | | 2,676 |
| Repurchases of common stock | (437) | (17,201) | | | | (17,638) |
| Redeemable non-controlling interest | | | | | (399) | (399) |
| **Balance at November 30, 2013** | 50,229 | 44,490 | 907,308 | (71,962) | 396 | 930,461 |
| Comprehensive income | | | 35,108 | 1,264 | 164 | 36,536 |
| Dividends | | | (11,105) | | | (11,105) |
| Stock option exercises | 216 | 4,435 | | | | 4,651 |
| Share-based compensation plans other, net | 64 | 7,405 | | | | 7,469 |
| Excess tax benefit on share-based compensation | | 2,450 | | | | 2,450 |
| Repurchases of common stock | (316) | (15,133) | | | | (15,449) |
| Redeemable non-controlling interest | | | | | (155) | (155) |
| **Balance at May 31, 2014** | **$ 50,193** | **$ 43,647** | **$ 931,311** | **$ (70,698)** | **$ 405** | **$ 954,858** |

See accompanying Notes to Condensed Consolidated Financial Statements.

**H.B. FULLER COMPANY AND SUBSIDIARIES**

**Condensed Consolidated Statements of Cash Flows**

(In thousands)

(Unaudited)

| | 26 Weeks Ended | |
|---|---|---|
| | **May 31, 2014** | **June 1, 2013** |
| **Cash flows from operating activities from continuing operations:** | | |
| Net income including non-controlling interests | **$ 35,275** | $ 46,822 |
| Adjustments to reconcile net income including non-controlling interests to net cash provided by (used in) operating activities from continuing operations: | | |
| Depreciation | **22,073** | 18,887 |
| Amortization | **11,578** | 11,101 |
| Deferred income taxes | **(586)** | (428) |
| (Income) from equity method investments, net of dividends received | **(3,537)** | 4,984 |
| Share-based compensation | **7,148** | 6,215 |
| Excess tax benefit from share-based compensation | **(2,450)** | (2,029) |
| Change in assets and liabilities, net of effects of acquisitions and discontinued operations: | | |
| Trade receivables, net | **(23,847)** | 1,152 |
| Inventories | **(60,635)** | (16,950) |
| Other assets | **(12,569)** | (8,959) |
| Trade payables | **27,122** | 1,046 |
| Accrued compensation | **(24,921)** | (11,951) |
| Other accrued expenses | **5,601** | (1,888) |
| Income taxes payable | **(3,990)** | (8,231) |
| Accrued / prepaid pensions | **(9,071)** | (1,499) |
| Other liabilities | **(3,211)** | (4,280) |
| Other | **2,180** | 6,719 |
| **Net cash provided by (used in) operating activities from continuing operations** | **(33,840)** | 40,711 |
| **Cash flows from investing activities from continuing operations:** | | |
| Purchased property, plant and equipment | **(82,142)** | (48,039) |
| Purchased businesses | **(151)** | 1,625 |
| Purchased technology | | (2,387) |
| Proceeds from sale of property, plant and equipment | **1,797** | 353 |
| **Net cash used in investing activities from continuing operations** | **(80,496)** | (48,448) |
| **Cash flows from financing activities from continuing operations:** | | |
| Proceeds from long-term debt | **175,000** | 95,000 |
| Repayment of long-term debt | **(110,000)** | (110,000) |
| Net proceeds (repayments) from notes payable | **9,039** | (5,807) |
| Dividends paid | **(11,024)** | (9,294) |
| Distribution to redeemable non-controlling interest | | (244) |

| | | |
|---|---|---|
| Proceeds from stock options exercised | **4,651** | 4,371 |
| Excess tax benefit from share-based compensation | **2,450** | 2,029 |
| Repurchases of common stock | **(15,449)** | (7,104) |
| **Net cash provided by (used in) financing activities from continuing operations** | **54,667** | (31,049) |
| Effect of exchange rate changes | **(408)** | (391) |
| **Net change in cash and cash equivalents from continuing operations** | **(60,077)** | (39,177) |
| Cash used in operating activities of discontinued operations | | (74) |
| **Net change in cash and cash equivalents** | **(60,077)** | (39,251) |
| Cash and cash equivalents at beginning of period | **155,121** | 200,436 |
| **Cash and cash equivalents at end of period** | **$ 95,044** | $ 161,185 |
| Supplemental disclosure of cash flow information: | | |
| Dividends paid with company stock | **$ 81** | $ 73 |
| Cash paid for interest, net of amount capitalized of $1,950 and $443 for the periods ended May 31, 2014 and June 1, 2013, respectively | **$ 11,844** | $ 11,999 |
| Cash paid for income taxes, net of refunds | **$ 9,493** | $ 20,406 |

See accompanying Notes to Condensed Consolidated Financial Statements.

**H.B. FULLER COMPANY AND SUBSIDIARIES**

**Notes to Condensed Consolidated Financial Statements**

(Amounts in thousands, except share and per share amounts)

(Unaudited)

**Note 1: Accounting Policies**

The accompanying unaudited interim Condensed Consolidated Financial Statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information necessary for a fair presentation of results of operations, comprehensive income, financial position, and cash flows in conformity with U.S. generally accepted accounting principles. In our opinion, the unaudited interim Condensed Consolidated Financial Statements reflect all adjustments of a normal recurring nature considered necessary for the fair presentation of the results for the periods presented. Operating results for interim periods are not necessarily indicative of results that may be expected for the fiscal year as a whole.

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses, and related disclosures at the date of the financial statements and during the reporting period. Actual results could differ from these estimates. These unaudited interim Condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and Notes thereto included in our Annual Report on Form 10-K for the year ended November 30, 2013 as filed with the Securities and Exchange Commission.

Cash and Cash Equivalents: We review cash and cash equivalent balances on a bank by bank basis to identify book overdrafts. Book overdrafts occur when the amount of outstanding checks exceed the cash deposited at a given bank. Book overdrafts, if any, are included in trade payables in our Condensed Consolidated Balance Sheets and in operating activities from continuing operations in our Condensed Consolidated Statement of Cash Flows.

**Recently Adopted Accounting Pronouncements:**

In February 2013, the FASB issued ASU No. 2013-02, Comprehensive Income: Reporting of Amounts Reclassified out of AOCI which further amended the disclosure requirements for comprehensive income. The update requires entities to disclose items reclassified out of accumulated other comprehensive income (AOCI) and into net income in a single location either in the notes to the Condensed Consolidated Financial Statements or parenthetically on the face of the Condensed Consolidated Statements of Income. The amendment is effective for fiscal years, and interim periods within those years, beginning after December 15, 2012 and is to be applied prospectively. We adopted the new requirements in the first quarter of our 2014 fiscal year. Since this update impacts disclosure requirements only, the adoption of this update did not have an impact on our condensed consolidated results of operations or financial condition.

In July 2013, the FASB issued ASU No. 2013-11, Income Taxes: Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists which requires that an unrecognized tax benefit should be presented in the financial statements as a reduction of a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward when settlement in this manner is available under the law. This guidance is effective for fiscal years and interim periods beginning after December 15, 2013 which is our fiscal 2015 and will be applied on a prospective basis to all unrecognized tax benefits that exist at the effective date. We adopted the new requirements in the first quarter of our 2014 fiscal year as early adoption was permitted. The adoption of this update did not have a material impact on our condensed consolidated financial condition.

**New Accounting Pronouncements:**

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The new standard is effective for fiscal years and interim periods beginning after December 15, 2016 which is our fiscal year beginning on December 3, 2017. Early application is not permitted. The standard permits the use of either the retrospective or cumulative effect transition method. We are evaluating the effect that ASU No. 2014-09 will have on our condensed consolidated financial statements and related disclosures. We have not yet selected a transition method nor have we determined the effect of the standard on our ongoing financial reporting.

**Note 2: Acquisitions and Divestitures**

**Acquisitions**

**Plexbond Quimica, S.A.:** On June 6, 2013 we acquired Plexbond Quimica, S.A., a provider of chemical urethane adhesives and polyester resins based in Curitiba, Brazil. The acquisition was a stock purchase and encompassed all of Plexbond Quimica, S.A. business operations. The purchase price of $10,390 was funded through existing cash and was recorded in our Americas Adhesives operating segment.

The following table summarizes the final fair value measurement of the assets acquired and liabilities assumed as of the date of acquisition:

| | Preliminary Valuation November 30, 2013 | Final Purchase Price Adjustment | Final Valuation May 31, 2014 |
|---|---|---|---|
| Current assets | $ 5,179 | $ | **$ 5,179** |
| Property, plant and equipment | 2,275 | | **2,275** |
| Goodwill | 3,626 | 151 | **3,777** |
| Other intangibles | | | |
| Customer relationships | 3,529 | | **3,529** |
| Noncompetition agreements | 565 | | **565** |
| Other assets | 608 | | **608** |
| Current liabilities | (3,684) | | **(3,684)** |
| Other liabilities | (1,859) | | **(1,859)** |
| Total purchase price | $ 10,239 | $ 151 | **$ 10,390** |

**Divestitures**

**Central America Paints:** On August 6, 2012 we completed the sale of our Central America Paints business to Compania Global de Pinturas S.A., a company of Inversiones Mundial S.A. The assets and liabilities of this business are presented on the Condensed Consolidated Balance Sheets as assets and liabilities of discontinued operations. A portion of the cash proceeds was determined to be contingent consideration, pending resolution of purchase agreement contingencies. The contingent consideration was valued at fair value based on level 3 inputs. The contingent consideration was included in current liabilities of discontinued operations in the Condensed Consolidated Balance Sheets at May 31, 2014 and November 30, 2013 as we expect the purchase agreement contingencies to be resolved in 2014.

The major classes of assets and liabilities of discontinued operations as of May 31, 2014 and November 30, 2013 were as follows:

| | May 31, 2014 | November 30, 2013 |
|---|---|---|
| Current assets of discontinued operations | **$ 1,865** | $ 1,865 |
| Current liabilities of discontinued operations | **$ 5,000** | $ 5,000 |

**Note 3: Accounting for Share-Based Compensation**

**Overview:** We have various share-based compensation programs, which provide for equity awards including stock options, restricted stock shares, restricted stock units and deferred compensation. These equity awards fall under several plans and are described in detail in our Annual Report on Form 10-K for the year ended November 30, 2013. Starting in 2014 we will no longer grant restricted stock shares.

**Grant-Date Fair Value:** We use the Black-Scholes option-pricing model to calculate the grant-date fair value of an award. The fair value of options granted during the 13 weeks and 26 weeks ended May 31, 2014 and June 1, 2013 were calculated using the following weighted average assumptions:

| | 13 Weeks Ended | | 26 Weeks Ended | |
|---|---|---|---|---|
| | **May 31, 2014** | **June 1, 2013** | **May 31, 2014** | **June 1, 2013** |
| Expected life (in years) | **4.75** | 4.75 | **4.75** | 4.75 |
| Weighted-average expected volatility | **32.70%** | 47.65% | **34.17%** | 48.00% |
| Expected volatility | **32.70%** | 47.65% | **32.70% 37.06%** | 47.65% 48.02% |
| Risk-free interest rate | **1.64%** | 0.69% | **1.51%** | 0.73% |
| Expected dividend yield | **0.84%** | 1.04% | **0.82%** | 0.87% |
| Weighted-average fair value of grants | **$13.33** | $14.27 | **$14.21** | $15.09 |

Expected life We use historical employee exercise and option expiration data to estimate the expected life assumption for the Black-Scholes grant-date valuation. We believe that this historical data is currently the best estimate of the expected term of a new option. We use a weighted-average expected life for all awards.

Expected volatility Volatility is calculated using our historical volatility for the same period of time as the expected life. We have no reason to believe that our future volatility will differ materially from the past.

Risk-free interest rate The rate is based on the U.S. Treasury yield curve in effect at the time of the grant for the same period of time as the expected life.

Expected dividend yield The calculation is based on the total expected annual dividend payout divided by the average stock price.

**Expense Recognition:** We use the straight-line attribution method to recognize share-based compensation expense for option awards with graded vesting and restricted stock share and restricted stock units with graded and cliff vesting. The amount of share-based compensation expense recognized during a period is based on the value of the portion of the awards that are ultimately expected to vest.

Total share-based compensation expense of $3,163 and $2,895 was included in our Condensed Consolidated Statements of Income for the 13 weeks ended May 31, 2014 and June 1, 2013, respectively. Total share-based compensation expense of $7,148 and $6,215 was included in our Condensed Consolidated Statements of Income for the 26 weeks ended May 31, 2014 and June 1, 2013, respectively. All share-based compensation expense was recorded as selling, general and administrative expense. For the 13 weeks ended May 31, 2014 and June 1, 2013 there was $837 and $225 of excess tax benefit recognized, respectively. For the 26 weeks ended May 31, 2014 and June 1, 2013 there was $2,450 and $2,029 of excess tax benefit recognized, respectively.

As of May 31, 2014, there was $9,717 of unrecognized compensation costs related to unvested stock option awards, which is expected to be recognized over a weighted-average period of 1.3 years. Unrecognized compensation costs related to unvested restricted stock shares was $5,164 which is expected to be recognized over a weighted-average period of 1.5 years. Unrecognized compensation costs related to unvested restricted stock units was $6,249 which is expected to be recognized over a weighted-average period of 1.4 years.

**Share-based Activity**

A summary of option activity as of May 31, 2014 and changes during the 26 weeks then ended is presented below:

| | Options | Weighted-Average Exercise Price |
|---|---|---|
| Outstanding at November 30, 2013 | 2,429,961 | $ 25.74 |
| Granted | 415,079 | 48.90 |
| Exercised | (215,641) | 21.57 |
| Forfeited or cancelled | (19,025) | 33.81 |
| Outstanding at May 31, 2014 | 2,610,374 | $ 29.71 |

The total fair values of options granted during the 13 weeks ended May 31, 2014 and June 1, 2013 were $106 and $277, respectively. Total intrinsic values of options exercised during the 13 weeks ended May 31, 2014 and June 1, 2013 were $3,119 and $533, respectively. Intrinsic value is the difference between our closing stock price on the respective trading day and the exercise price, multiplied by the number of options exercised. The total fair values of options granted during the 26 weeks ended May 31, 2014 and June 1, 2013 were $5,899 and $6,823, respectively. Total intrinsic values of options exercised during the 26 weeks ended May 31, 2014 and June 1, 2013 were $5,792 and $4,770, respectively. Proceeds received from option exercises during the 13 weeks ended May 31, 2014 and June 1, 2013 were $2,646 and $597, respectively and $4,651 and $4,371 during the 26 weeks ended May 31, 2014 and June 1, 2013, respectively.

A summary of nonvested restricted stock as of May 31, 2014 and changes during the 26 weeks then ended is presented below:

| | **Units** | **Shares** | **Total** | **Weighted-Average Grant Date Fair Value** | **Weighted-Average Remaining Contractual Life (in Years)** |
|---|---|---|---|---|---|
| Nonvested at November 30, 2013 | 135,231 | 312,445 | 447,676 | $ 33.76 | 1.2 |
| Granted | 124,387 | | 124,387 | 48.89 | 1.7 |
| Vested | (65,911) | (111,291) | (177,202) | 48.20 | |
| Forfeited | (335) | (6,161) | (6,496) | 35.43 | 1.3 |
| Nonvested at May 31, 2014 | 193,372 | 194,993 | 388,365 | $ 40.49 | 1.4 |

Total fair values of restricted stock vested during the 13 weeks ended May 31, 2014 and June 1, 2013 were $251 and $278, respectively. Total fair values of restricted stock vested during the 26 weeks ended May 31, 2014 and June 1, 2013 were $8,541 and $6,550, respectively. The total fair value of nonvested restricted stock at May 31, 2014 was $11,413.

We repurchased 2,249 and 1,972 restricted stock shares during the 13 weeks ended May 31, 2014 and June 1, 2013, respectively and 66,312 and 61,624 during the 26 weeks ended May 31, 2014 and June 1, 2013, respectively The repurchases relate to statutory minimum tax withholding.

We have a Directors Deferred Compensation plan that allows non-employee directors to defer all or a portion of their directors compensation in a number of investment choices, including units representing shares of our common stock. We also have a Key Employee Deferred Compensation Plan that allows key employees to defer a portion of their eligible compensation in a number of investment choices, including units, representing shares of our common stock. We provide a 10 percent match on deferred compensation invested into units, representing shares of our common stock. A summary of deferred compensation units as of May 31, 2014, and changes during the 26 weeks then ended is presented below:

**Non-employee**

| | Directors | Employees | Total |
|---|---|---|---|
| Units outstanding November 30, 2013 | 312,680 | 61,288 | 373,968 |
| Participant contributions | 6,556 | 1,212 | 7,768 |
| Company match contributions | 656 | 121 | 777 |
| Payouts | (298) | (7,257) | (7,555) |
| Units outstanding May 31, 2014 | 319,594 | 55,364 | 374,958 |

Deferred compensation units are fully vested at the date of contribution.

**Note 4: Earnings Per Share**

A reconciliation of the common share components for the basic and diluted earnings per share calculations follows:

| | 13 Weeks Ended | | 26 Weeks Ended | |
|---|---|---|---|---|
| (Shares in thousands) | **May 31, 2014** | **June 1, 2013** | **May 31, 2014** | **June 1, 2013** |
| Weighted-average common shares basic | **49,956** | 49,935 | **49,933** | 49,876 |
| Equivalent shares from share-based compensations plans | **1,219** | 1,217 | **1,282** | 1,214 |
| Weighted-average common and common equivalent shares diluted | **51,175** | 51,152 | **51,215** | 51,090 |

Basic earnings per share is calculated by dividing net income attributable to H.B. Fuller by the weighted-average number of common shares outstanding during the applicable period. Diluted earnings per share is based upon the weighted-average number of common and common equivalent shares outstanding during the applicable period. The difference between basic and diluted earnings per share is attributable to share-based compensation awards. We use the treasury stock method to calculate the effect of outstanding shares, which computes total employee proceeds as the sum of (a) the amount the employee must pay upon exercise of the award, (b) the amount of unearned share-based compensation costs attributed to future services and (c) the amount of tax benefits, if any, that would be credited to additional paid-in capital assuming exercise of the award. Share-based compensation awards for which total employee proceeds exceed the average market price over the applicable period have an antidilutive effect on earnings per share, and accordingly, are excluded from the calculation of diluted earnings per share.

Options to purchase 407,145 shares of common stock at a weighted-average exercise price of $48.93 for the 13 weeks and 26 weeks ended May 31, 2014, were excluded from the diluted earnings per share calculations because they were antidilutive. Our 2013 first and second quarter-end stock prices were higher than any of our stock option grant prices at that time, therefore no option shares were excluded from the diluted earnings per share calculations for the second quarter and first six months of 2013.

**Note 5: Accumulated Other Comprehensive Income (Loss)**

The following table provides details of total comprehensive income (loss):

| | **13 Weeks Ended May 31, 2014** | | | | 13 Weeks Ended June 1, 2013 | | | |
|---|---|---|---|---|---|---|---|---|
| | **H.B. Fuller Stockholders** | | | **Non-controlling Interests** | H.B. Fuller Stockholders | | | Non-controlling Interests |
| | **Pretax** | **Tax** | **Net** | **Net** | Pretax | Tax | Net | Net |
| **Net income including non-controlling interests** | | | **$ 20,537** | **$ 89** | | | $ 25,929 | $ 119 |
| Other comprehensive income (loss) | | | | | | | | |
| Foreign currency translation adjustment[1] | **$ (1,385)** | | **(1,385)** | **8** | $ (5,601) | | (5,601) | (46) |
| Reclassification to earnings: | | | | | | | | |
| | **1,670** | **(649)** | **1,021** | | 3,026 | (1,061) | 1,965 | |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Defined benefit pension plans adjustment[2] | | | | | | | | |
| Interest rate swap[3] | **14** | **(4)** | **10** | | 14 | (4) | 10 | |
| Cash-flow hedges[3] | **47** | **(18)** | **29** | | (34) | 13 | (21) | |
| **Other comprehensive income (loss)** | **$ 346** | **$ (671)** | **(325)** | **8** | $ (2,595) | $ (1,052) | (3,647) | (46) |
| Comprehensive income | | | **$ 20,212** | **$ 97** | | | $ 22,282 | $ 73 |

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| | 26 Weeks Ended May 31, 2014 | | | | 26 Weeks Ended June 1, 2013 | | | |
|---|---|---|---|---|---|---|---|---|
| | H.B. Fuller Stockholders | | | Non-controlling Interests | H.B. Fuller Stockholders | | | Non-controlling Interests |
| | Pretax | Tax | Net | Net | Pretax | Tax | Net | Net |
| **Net income including non-controlling interests** | | | **$ 35,108** | **$ 167** | | | $ 46,606 | $ 216 |
| Other comprehensive income (loss) | | | | | | | | |
| Foreign currency translation adjustment[1] | **$ (827)** | | **(827)** | **(3)** | $ (9,070) | | (9,070) | (39) |
| Reclassification to earnings: | | | | | | | | |
| Defined benefit pension plans adjustment[2] | **3,326** | **(1,287)** | **2,039** | | 6,067 | (2,126) | 3,941 | |
| Interest rate swap[3] | **28** | **(8)** | **20** | | 28 | (8) | 20 | |
| Cash-flow hedges[3] | **53** | **(21)** | **32** | | 308 | (119) | 189 | |
| **Other comprehensive income (loss)** | **$ 2,580** | **$ (1,316)** | **1,264** | **(3)** | $ (2,667) | $ (2,253) | (4,920) | (39) |
| Comprehensive income | | | **$ 36,372** | **$ 164** | | | $ 41,686 | $ 177 |

1 Income taxes are not provided for foreign currency translation relating to permanent investments in international subsidiaries.

2 Loss reclassified from AOCI into earnings as part of net periodic cost related to pension and other postretirement benefit plans is reported in cost of sales, SG&A and special charges.

3 Loss reclassified from AOCI into earnings is reported in other income (expense), net.

The components of accumulated other comprehensive income (loss) follow:

| | May 31, 2014 | | |
|---|---|---|---|
| | **Total** | **H.B. Fuller Stockholders** | **Non-controlling Interests** |
| Foreign currency translation adjustment | **$ 49,041** | **$ 49,051** | **$ (10)** |
| Defined benefit pension plans adjustment, net of taxes of $63,923 | **(119,616)** | **(119,616)** | |
| Interest rate swap, net of taxes of $28 | **(74)** | **(74)** | |
| Cash-flow hedges, net of taxes of $36 | **(59)** | **(59)** | |
| Accumulated other comprehensive income (loss) | **$ (70,708)** | **$ (70,698)** | **$ (10)** |

| | November 30, 2013 | | |
|---|---|---|---|
| | **Total** | **H.B. Fuller Stockholders** | **Non-controlling Interests** |
| Foreign currency translation adjustment | $ 49,871 | $ 49,878 | $ (7) |
| | (121,655) | (121,655) | |

| | | | | | | |
|---|---|---|---|---|---|---|
| Defined benefit pension plans adjustment, net of taxes of $65,210 | | | | | | |
| Interest rate swap, net of taxes of $36 | | (94) | | (94) | | |
| Cash-flow hedges, net of taxes of $57 | | (91) | | (91) | | |
| Accumulated other comprehensive income (loss) | $ | (71,969) | $ | (71,962) | $ | (7) |

**Note 6: Special Charges, net**

The integration of the Forbo industrial adhesives business we acquired in March 2012 involves a significant amount of restructuring and capital investment to optimize the new combined entity. In addition, we are taking a series of actions in our existing EIMEA operating segment to improve the profitability and future growth prospects of this operating segment. We have combined these two initiatives into a single project which we refer to as the Business Integration Project . During the 13 weeks ended May 31, 2014 and June 1, 2013, we incurred special charges, net of $13,538 and $10,843, respectively and $25,272 and $16,176 for the 26 weeks ended May 31, 2014 and June 1, 2013, respectively for costs related to the Business Integration Project.

The following table provides detail of special charges, net:

| | 13 Weeks Ended | | 26 Weeks Ended | |
|---|---|---|---|---|
| | **May 31, 2014** | **June 1, 2013** | **May 31, 2014** | **June 1, 2013** |
| Acquisition and transformation related costs | **$ 2,578** | $ 1,884 | **$ 4,286** | $ 4,166 |
| Workforce reduction costs | **899** | 3,697 | **2,958** | 4,181 |
| Facility exit costs | **7,326** | 3,267 | **12,452** | 5,056 |
| Other related costs | **2,735** | 1,995 | **5,576** | 2,773 |
| Special charges, net | **$ 13,538** | $ 10,843 | **$ 25,272** | $ 16,176 |

Acquisition and transformation related costs of $2,578 for the 13 weeks ended May 31, 2014 and $1,884 for the 13 weeks ended June 1, 2013 include costs related to organization consulting, financial advisory and legal services necessary to integrate the Forbo industrial adhesives business into our existing operating segments. For the 26 weeks ended May 31, 2014 and June 1, 2013 we incurred acquisition and transformation related costs of $4,286 and $4,166, respectively. During the 13 weeks ended May 31, 2014, we incurred workforce reduction costs of $899, cash facility exit costs of $5,708 and non-cash facility exit costs of $1,618 and other incremental transformation related costs of $2,735 including the cost of personnel directly working on the integration. During the 26 weeks ended May 31, 2014, we incurred workforce reduction costs of $2,958, cash facility exit costs of $9,282 and non-cash facility exit costs of $3,170 and other incremental transformation related costs of $5,576 including the cost of personnel directly working on the integration. During the 13 weeks and 26 weeks ended June 1, 2013, we incurred workforce reduction costs of $3,697 and 4,181, respectively, cash facility exit costs of $2,316 and $3,714, respectively, non-cash facility exit costs of $951 and $1,342, respectively and other incremental transformation related costs of $1,995 and $2,773, respectively including the cost of personnel directly working on the integration.

For the 26 weeks ended May 31, 2014, the activity in accrued compensation associated with the Business Integration Project, is as follows:

| | **Workforce Reduction Costs** |
|---|---|
| Balance at November 30, 2013 | $ 18,057 |
| Workforce reduction costs | 2,958 |
| Cash payments | (13,433) |
| Foreign currency translation adjustment | (53) |

| | | |
|---|---|---|
| Balance at May 31, 2014 | $ | 7,529 |

Of the $7,529 in accrued workforce reduction costs at May 31, 2014, $6,654 was included in accrued compensation and $875 was included in other liabilities on our Condensed Consolidated Balance Sheets as this portion was not expected to be paid within the next year. The benefits were accrued based primarily on the formal severance plans in place for the various locations. The special charges are not allocated to our operating segments.

**Note 7: Components of Net Periodic Cost (Benefit) related to Pension and Other Postretirement Benefit Plans**

| | 13 Weeks Ended May 31, 2014 and June 1, 2013 | | | | | |
|---|---|---|---|---|---|---|
| | Pension Benefits | | | | Other Postretirement Benefits | |
| | U.S. Plans | | Non-U.S. Plans | | | |
| Net periodic cost (benefit): | **2014** | **2013** | **2014** | **2013** | **2014** | **2013** |
| Service cost | **$ 24** | $ 27 | **$ 438** | $ 416 | **$ 109** | $ 156 |
| Interest cost | **4,021** | 3,680 | **1,924** | 1,820 | **536** | 533 |
| Expected return on assets | **(5,967)** | (5,680) | **(2,736)** | (2,318) | **(1,185)** | (931) |
| Amortization: | | | | | | |
| Prior service cost | **7** | 12 | **(1)** | (1) | **(943)** | (1,034) |
| Actuarial (gain)/ loss | **1,144** | 1,685 | **784** | 935 | **678** | 1,429 |
| Net periodic cost (benefit) | **$ (771)** | $ (276) | **$ 409** | $ 852 | **$ (805)** | $ 153 |

| | 26 Weeks Ended May 31, 2014 and June 1, 2013 | | | | | |
|---|---|---|---|---|---|---|
| | Pension Benefits | | | | Other Postretirement Benefits | |
| | U.S. Plans | | Non-U.S. Plans | | | |
| Net periodic cost (benefit): | **2014** | **2013** | **2014** | **2013** | **2014** | **2013** |
| Service cost | **$ 47** | $ 54 | **$ 868** | $ 839 | **$ 217** | $ 312 |
| Interest cost | **8,043** | 7,360 | **3,817** | 3,689 | **1,072** | 1,066 |
| Expected return on assets | **(11,933)** | (11,360) | **(5,426)** | (4,700) | **(2,371)** | (1,862) |
| Amortization: | | | | | | |
| Prior service cost | **14** | 24 | **(2)** | (2) | **(1,886)** | (2,068) |
| Actuarial (gain)/ loss | **2,288** | 3,370 | **1,556** | 1,886 | **1,355** | 2,858 |
| Net periodic cost (benefit) | **$ (1,541)** | $ (552) | **$ 813** | $ 1,712 | **$ (1,613)** | $ 306 |

**Note 8: Inventories**

The composition of inventories follows:

| | **May 31, 2014** | **November 30, 2013** |
|---|---|---|
| Raw materials | **$ 148,625** | $ 119,536 |
| Finished goods | **153,919** | 122,584 |
| LIFO reserve | **(20,630)** | (20,583) |
| Total inventories | **$ 281,914** | $ 221,537 |

**Note 9: Financial Instruments**

As a result of being a global enterprise, our earnings, cash flows and financial position are exposed to foreign currency risk from foreign currency denominated receivables and payables. These items are denominated in various foreign currencies, including the Euro, British pound sterling, Canadian dollar, Chinese renminbi, Japanese yen, Australian dollar, Argentine peso, Brazilian real, Colombian peso, Mexican peso, Turkish lira, Egyptian pound, Indian rupee and Malaysian ringgit.

Our objective is to balance, where possible, local currency denominated assets to local currency denominated liabilities to have a natural hedge and minimize foreign exchange impacts. We take steps to minimize risks from foreign currency exchange rate fluctuations through normal operating and financing activities and, when deemed appropriate, through the use of derivative instruments. We do not enter into any speculative positions with regard to derivative instruments.

We enter into derivative contracts with a group of investment grade multinational commercial banks. We evaluate the credit quality of each of these banks on a periodic basis as warranted.

Effective March 5, 2012, we entered into a cross-currency swap agreement to convert a notional amount of $98,738 of foreign currency denominated intercompany loans into US dollars. The swap matures in 2015. As of May 31, 2014, the fair value of the swap was a liability of $3,594 and was included in other liabilities in the Condensed Consolidated Balance Sheets. The swap was designated as cash-flow hedges for accounting treatment. The lesser amount between the cumulative change in the fair value of the actual swap and the cumulative change in the fair value of hypothetical swap is recorded in accumulated other comprehensive income (loss) in the Condensed Consolidated Balance Sheets. The difference between the cumulative change in the fair value of the actual swap and the cumulative change in the fair value of hypothetical swap is recorded as other income (expense), net in the Condensed Consolidated Statements of Income. In a perfectly effective hedge relationship, the two fair value calculations would exactly offset each other. Any difference in the calculation represents hedge ineffectiveness. The ineffectiveness calculations as of May 31, 2014 resulted in additional pre-tax loss of $23 year-to-date as the change in fair value of the cross-currency swap was less than the change in the fair value of the hypothetical swap. The amount in accumulated other comprehensive income (loss) related to cross-currency swap was a loss of $59 at May 31, 2014. The estimated net amount of the existing loss that is reported in accumulated other comprehensive income (loss) at May 31, 2014 that is expected to be reclassified into earnings within the next twelve months is $59. At May 31, 2014, we believe the original forecasted transactions will occur, therefore, we do not believe any gains or losses will be reclassified into earnings as a result of the discontinuance of this cash flow hedge.

The following table summarizes the cross-currency swap outstanding as of May 31, 2014:

| | **Fiscal Year of Expiration** | **Interest Rate** | **Notional Value** | **Fair Value** |
|---|---|---|---|---|
| Pay EUR | 2015 | 4.30% | $ 98,738 | $ (3,594) |
| Receive USD | | 4.45% | | |

Except for the cross currency swap agreement listed above, foreign currency derivative instruments outstanding are not designated as hedges for accounting purposes. The gains and losses related to mark-to-market adjustments are recognized as other income or expense in the income statement during the periods in which the derivative instruments are outstanding. See Note 14 to Condensed Consolidated Financial Statements for fair value amounts of these derivative instruments.

As of May 31, 2014, we had forward foreign currency contracts maturing between June 6, 2014 and November 3, 2014. The mark-to-market effect associated with these contracts, on a net basis, was a gain of $2 at May 31, 2014. These losses were largely offset by the underlying transaction gains and losses resulting from the foreign currency exposures for which these contracts relate.

We have interest rate swap agreements to convert $75,000 of our Senior Notes to variable interest rates. The change in fair value of the Senior Notes, attributable to the change in the risk being hedged, was a liability of $5,334 at May 31, 2014 and was included in long-term debt in the Condensed Consolidated Balance Sheets. The fair values of the swaps in total were an asset of $5,293 at May 31, 2014 and were included in other assets in the Condensed Consolidated Balance Sheets. The swaps were designated for hedge accounting treatment as fair value hedges. The changes in the fair value of the swap and the fair value of the Senior Notes attributable to the change in the risk being hedged are recorded as other income (expense), net in the Condensed Consolidated Statements of Income. In a perfectly effective hedge relationship, the two fair value calculations would exactly offset each other. Any difference in the calculation represents hedge ineffectiveness. The calculation as of May 31, 2014 resulted in additional pre-tax gain of $94 year-to-date as the fair value of the interest rate swaps increased by more than the change in the fair value of the Senior Notes attributable to the change in the risk being hedged.

Concentrations of credit risk with respect to trade accounts receivable are limited due to the large number of entities in the customer base and their dispersion across many different industries and countries. As of May 31, 2014, there were no significant concentrations of credit risk.

**Note 10: Commitments and Contingencies**

**Environmental Matters:** From time to time, we become aware of compliance matters relating to, or receive notices from, federal, state or local entities regarding possible or alleged violations of environmental, health or safety laws and regulations. We review the circumstances of each individual site, considering the number of parties involved, the level of potential liability or contribution of us relative to the other parties, the nature and magnitude of the hazardous substances involved, the method and extent of remediation, the estimated legal and consulting expense with respect to each site and the time period over which any costs would likely be incurred. Also, from time to time, we are identified as a potentially responsible party (PRP) under the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) and/or similar state laws that impose liability for costs relating to the clean up of contamination resulting from past spills, disposal or other release of hazardous substances. We are also subject to similar laws in some of the countries where current and former facilities are located. Our environmental, health and safety department monitors compliance with applicable laws on a global basis. To the extent we can reasonably estimate the amount of our probable liabilities for environmental matters, we establish a financial provision.

Currently we are involved in various environmental investigations, clean up activities and administrative proceedings and lawsuits. In particular, we are currently deemed a PRP in conjunction with numerous other parties, in a number of government enforcement actions associated with landfills and/or hazardous waste sites. As a PRP, we may be required to pay a share of the costs of investigation and clean up of these sites. In addition, we are engaged in environmental remediation and monitoring efforts at a number of current and former operating facilities. While uncertainties exist with respect to the amounts and timing of the ultimate environmental liabilities, based on currently available information, we have concluded that these matters, individually or in the aggregate, will not have a material adverse effect on our results of operations, financial condition or cash flow.

**Other Legal Proceedings:** From time to time and in the ordinary course of business, we are a party to, or a target of, lawsuits, claims, investigations and proceedings, including product liability, personal injury, contract, patent and intellectual property, environmental, health and safety, tax and employment matters. While we are unable to predict the outcome of these matters, we have concluded, based upon currently available information, that the ultimate resolution of any pending matter, individually or in the aggregate, including the asbestos litigation described in the following paragraphs, will not have a material adverse effect on our results of operations, financial condition or cash flow.

We have been named as a defendant in lawsuits in which plaintiffs have alleged injury due to products containing asbestos manufactured more than 30 years ago. The plaintiffs generally bring these lawsuits against multiple defendants and seek damages (both actual and punitive) in very large amounts. In many cases, plaintiffs are unable to demonstrate that they have suffered any compensable injuries or that the injuries suffered were the result of exposure to products manufactured by us. We are typically dismissed as a defendant in such cases without payment. If the plaintiff presents evidence indicating that compensable injury occurred as a result of exposure to our products, the case is generally settled for an amount that reflects the seriousness of the injury, the length, intensity and character of exposure to products containing asbestos, the number and solvency of other defendants in the case, and the jurisdiction in which the case has been brought.

A significant portion of the defense costs and settlements in asbestos-related litigation is paid by third parties, including indemnification pursuant to the provisions of a 1976 agreement under which we acquired a business from a third party. Currently, this third party is defending and paying settlement amounts, under a reservation of rights, in most of the asbestos cases tendered to the third party.

In addition to the indemnification arrangements with third parties, we have insurance policies that generally provide coverage for asbestos liabilities (including defense costs). Historically, insurers have paid a significant portion of our defense costs and settlements in asbestos-related litigation. However, certain of our insurers are insolvent. We have entered into cost-sharing agreements with our insurers that provide for the allocation of defense costs and under certain circumstances, settlements and judgments, in asbestos-related lawsuits. Under these agreements, we are required under certain circumstances to fund a share of settlements and judgments allocable to years in which the responsible insurer is insolvent. In addition, to delineate our rights under certain insurance policies, in October 2009, we commenced a declaratory judgment action against one of our insurers in the United States District Court for the District of Minnesota. Additional insurers have been brought into the action to address issues related to the scope of their coverage. We recently entered into a settlement agreement with the defendant insurers in this case that provided for the allocation of defense costs and settlements in the future. The allocation under the settlement agreement depends on the outcome of an appeal of two issues to the United States Eighth Circuit Court of Appeals.

A summary of the number of and settlement amounts for asbestos-related lawsuits and claims is as follows:

| ($ in thousands) | 26 Weeks Ended May 31, 2014 | 26 Weeks Ended June 1, 2013 | 3 Years Ended November 30, 2013 |
|---|---|---|---|
| Lawsuits and claims settled | **4** | | 22 |
| Settlement amounts | **$ 178** | $ | $ 1,448 |
| Insurance payments received or expected to be received | **$ 155** | $ | $ 1,087 |

We do not believe that it would be meaningful to disclose the aggregate number of asbestos-related lawsuits filed against us because relatively few of these lawsuits are known to involve exposure to asbestos-containing products that we manufactured. Rather, we believe it is more meaningful to disclose the number of lawsuits that are settled and result in a payment to the plaintiff. To the extent we can reasonably estimate the amount of our probable liabilities for pending asbestos-related claims, we establish a financial provision and a corresponding receivable for insurance recoveries.

Based on currently available information, we have concluded that the resolution of any pending matter, including asbestos-related litigation, individually or in the aggregate, will not have a material adverse effect on our results of operations, financial condition or cash flow.

**Note 11: Operating Segments**

We are required to report segment information in the same way that we internally organize our business for assessing performance and making decisions regarding allocation of resources. We evaluate the performance of each of our operating segments based on segment operating income, which is defined as gross profit less selling, general and administrative (SG&A) expenses. Segment operating income excludes special charges, net. Corporate expenses are fully allocated to each operating segment. Inter-segment revenues are recorded at cost plus a markup for administrative costs. Operating results of each segment are regularly reviewed by our chief operating decision maker to make decisions about resources to be allocated to the segments and assess their performance.

Through the third quarter of 2013, our business was reported in five operating segments: North America Adhesives, EIMEA (Europe, India, Middle East and Africa), Latin America Adhesives, Asia Pacific and Construction Products. Changes in our management reporting structure during the fourth quarter of 2013 required us to conduct an operating segment assessment in accordance with ASC Topic 280 Segment Reporting , to determine our reportable segments. As a result of this assessment, we now have four reportable segments: Americas Adhesives, EIMEA, Asia Pacific and Construction Products. Prior periods have been restated to reflect our new operating segments.

The tables below provide certain information regarding net revenue and segment operating income of each of our operating segments:

| | 13 Weeks Ended | | | | | |
|---|---|---|---|---|---|---|
| | May 31, 2014 | | | June 1, 2013 | | |
| | Trade Revenue | Inter-Segment Revenue | Segment Operating Income | Trade Revenue | Inter-Segment Revenue | Segment Operating Income |
| Americas Adhesives | **$ 236,985** | **$ 5,774** | **$ 31,889** | $ 228,773 | $ 5,198 | $ 31,825 |
| EIMEA | **189,656** | **4,427** | **10,156** | 185,194 | 2,793 | 14,145 |

| | | | | | | |
|---|---|---|---|---|---|---|
| Asia Pacific | **67,948** | **3,107** | **1,758** | 62,115 | 3,788 | 2,793 |
| Construction Products | **49,445** | **691** | **2,480** | 42,934 | 134 | 4,047 |
| Total | **$ 544,034** | | **$ 46,283** | $ 519,016 | | $ 52,810 |

| | 26 Weeks Ended | | | | | |
|---|---|---|---|---|---|---|
| | **May 31, 2014** | | | **June 1, 2013** | | |
| | **Trade Revenue** | **Inter-Segment Revenue** | **Segment Operating Income** | **Trade Revenue** | **Inter-Segment Revenue** | **Segment Operating Income** |
| Americas Adhesives | **$ 446,651** | **$ 11,453** | **$ 57,095** | $ 436,504 | $ 10,076 | $ 57,750 |
| EIMEA | **361,215** | **8,533** | **18,596** | 362,695 | 5,469 | 20,618 |
| Asia Pacific | **132,995** | **6,579** | **3,546** | 122,694 | 7,279 | 4,767 |
| Construction Products | **89,154** | **963** | **3,292** | 76,965 | 215 | 5,411 |
| Total | **$ 1,030,015** | | **$ 82,529** | $ 998,858 | | $ 88,546 |

Reconciliation of segment operating income to income before income taxes and income from equity method investments:

| | 13 Weeks Ended | | 26 Weeks Ended | |
|---|---|---|---|---|
| | **May 31, 2014** | **June 1, 2013** | **May 31, 2014** | **June 1, 2013** |
| Segment operating income | **$ 46,283** | $ 52,810 | **$ 82,529** | $ 88,546 |
| Special charges, net | **(13,538)** | (10,843) | **(25,272)** | (16,176) |
| Other income (expense), net | **(204)** | (1,814) | **(1,254)** | (1,436) |
| Interest expense | **(4,760)** | (4,884) | **(8,886)** | (10,211) |
| Income before income taxes and income from equity method investments | **$ 27,781** | $ 35,269 | **$ 47,117** | $ 60,723 |

**Note 12: Income Taxes**

As of May 31, 2014, we had a $5,295 liability recorded under FASB ASC 740, Income Taxes for gross unrecognized tax benefits, excluding interest. As of May 31, 2014, we had accrued $613 of gross interest relating to unrecognized tax benefits. During the second quarter of 2014 our recorded liability for gross unrecognized tax benefits decreased by $48.

**Note 13: Goodwill**

A summary of goodwill activity for the first six months of 2014 is presented below:

| | |
|---|---|
| Balance at November 30, 2013 | $ 263,103 |
| Plexbond Quimica, S.A. acquisition (Note 2) | 151 |
| Currency impact | 1,135 |
| Balance at May 31, 2014 | $ 264,389 |

**Note 14: Fair Value Measurements**

The following tables present information about our financial assets and liabilities that are measured at fair value on a recurring basis as of May 31, 2014 and November 30, 2013, and indicates the fair value hierarchy of the valuation techniques utilized to determine such fair value. The hierarchy is broken down into three levels. Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 inputs include data points that are observable such as quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, and inputs (other than quoted prices) such as interest rates and yield curves that are observable for the asset or liability, either directly or indirectly. Level 3 inputs are unobservable data points for the asset or liability, and include situations where there is little, if any, market activity for the asset or liability.

| | May 31, | Fair Value Measurements Using: |
|---|---|---|

| Description | 2014 | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| Assets: | | | | |
| Marketable securities | **$ 1,271** | **$ 1,271** | **$** | **$** |
| Derivative assets | **956** | | **956** | |
| Interest rate swaps | **5,293** | | **5,293** | |
| Liabilities: | | | | |
| Derivative liabilities | **$ 954** | **$** | **$ 954** | **$** |
| Cash-flow hedges | **3,594** | | **3,594** | |