

RPM INTERNATIONAL INC/DE/

Form 10-Q

January 08, 2009

**Table of Contents**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**Form 10-Q**

- ☐ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**  
**For the quarterly period ended November 30, 2008,**
- 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 No. 1-14187**

**RPM International Inc.**

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

**DELAWARE**

*(State or other jurisdiction of  
incorporation or organization)*

**02-0642224**

*(IRS Employer  
Identification No.)*

**P.O. BOX 777;  
2628 PEARL ROAD;  
MEDINA, OHIO**

*(Address of principal executive offices)*

**44258**

*(Zip Code)*

**(330) 273-5090**

*(Registrant's telephone number including area code)*

**Not Applicable**

*(Former name, former address and former fiscal year, if changed since last report)*

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

Indicate by check mark whether the registrant 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 ☐

Accelerated filer ☐

Non-accelerated filer ☐

Smaller reporting  
company ☐

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(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 ☒.

As of January 6, 2009

128,410,957 Shares of RPM International Inc. Common Stock were outstanding.

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**RPM INTERNATIONAL INC. AND SUBSIDIARIES\***

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\* As used herein, the terms "RPM" and the "Company" refer to RPM International Inc. and its subsidiaries, unless the context indicates otherwise.

Table of Contents**PART I. FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****RPM INTERNATIONAL INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS**

|   | November 30,<br>2008<br>(Unaudited)<br>(In thousands, except per share<br>amounts) | May 31, 2008        |
|---|--|---------------------|
| <b><u>ASSETS</u></b>  |  |                     |
| <b>Current Assets</b>   |  |                     |
| Cash and short-term investments   | \$ 205,289   | \$ 231,251          |
| Trade accounts receivable (less allowances of \$20,464 and \$24,554,<br>respectively) | 607,189  | 817,241             |
| Inventories   | 493,241  | 476,149             |
| Deferred income taxes   | 36,974   | 37,644              |
| Prepaid expenses and other current assets   | 194,596  | 221,690             |
| <b>Total current assets</b>   | <b>1,537,289</b>   | <b>1,783,975</b>    |
| <b>Property, Plant and Equipment, at Cost</b>   | <b>1,007,208</b>   | <b>1,054,719</b>    |
| Allowance for depreciation and amortization   | (552,053)  | (556,998)           |
| <b>Property, plant and equipment, net</b>   | <b>455,155</b>   | <b>497,721</b>      |
| <b>Other Assets</b>   |  |                     |
| Goodwill  | 844,980  | 908,358             |
| Other intangible assets, net of amortization  | 348,770  | 384,370             |
| Other   | 167,008  | 189,143             |
| <b>Total other assets</b>   | <b>1,360,758</b>   | <b>1,481,871</b>    |
| <b>Total Assets</b>   | <b>\$ 3,353,202</b>  | <b>\$ 3,763,567</b> |
| <b><u>LIABILITIES AND STOCKHOLDERS' EQUITY</u></b>                                    |  |                     |
| <b>Current Liabilities</b>  |  |                     |
| Accounts payable  | \$ 282,429   | \$ 411,448          |
| Current portion of long-term debt   | 171,247  | 6,934               |
| Accrued compensation and benefits   | 102,716  | 151,493             |
| Accrued loss reserves   | 73,673   | 71,981              |

|   |                     |                     |
|---|---------------------|---------------------|
| Asbestos-related liabilities  | 65,000              | 65,000              |
| Other accrued liabilities   | 126,106             | 139,505             |
| <b>Total current liabilities</b>  | <b>821,171</b>      | <b>846,361</b>      |
| <b>Long-Term Liabilities</b>  |                     |                     |
| Long-term debt, less current maturities   | 791,364             | 1,066,687           |
| Asbestos-related liabilities  | 462,309             | 494,745             |
| Other long-term liabilities   | 137,884             | 192,412             |
| Deferred income taxes   | 19,729              | 26,806              |
| <b>Total long-term liabilities</b>  | <b>1,411,286</b>    | <b>1,780,650</b>    |
| <b>Stockholders' Equity</b>   |                     |                     |
| Preferred stock, par value \$0.01; authorized 50,000 shares; none issued  |                     |                     |
| Common stock, par value \$0.01 authorized 300,000 shares; issued and outstanding 128,381 as of November 2008; issued and outstanding 122,189 as of May 2008 | 1,284               | 1,222               |
| Paid-in capital   | 775,459             | 612,441             |
| Treasury stock, at cost   | (50,279)            | (6,057)             |
| Accumulated other comprehensive income (loss)   | (94,280)            | 101,162             |
| Retained earnings   | 488,561             | 427,788             |
| <b>Total stockholders' equity</b>   | <b>1,120,745</b>    | <b>1,136,556</b>    |
| <b>Total Liabilities and Stockholders' Equity</b>   | <b>\$ 3,353,202</b> | <b>\$ 3,763,567</b> |

The accompanying notes to consolidated financial statements are an integral part of these statements.

Table of Contents**RPM INTERNATIONAL INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF INCOME**

|  | <b>Three Months Ended</b>                       |                     | <b>Six Months Ended</b> |                     |
|--|---|---------------------|-------------------------|---------------------|
|  | <b>November 30,</b>                             | <b>November 30,</b> | <b>November 30,</b>     | <b>November 30,</b> |
|  | <b>2008</b>                                     | <b>2007</b>         | <b>2008</b>             | <b>2007</b>         |
|  | <b>(Unaudited)</b>                              |                     |                         |                     |
|  | <b>(In thousands, except per share amounts)</b> |                     |                         |                     |
| <b>Net Sales</b>   | <b>\$ 889,965</b>                               | <b>\$ 905,708</b>   | <b>\$ 1,875,430</b>     | <b>\$ 1,836,047</b> |
| <b>Cost of Sales</b>   | <b>533,239</b>                                  | <b>537,970</b>      | <b>1,115,115</b>        | <b>1,084,407</b>    |
| <b>Gross Profit</b>  | <b>356,726</b>                                  | <b>367,738</b>      | <b>760,315</b>          | <b>751,640</b>      |
| <b>Selling, General and Administrative Expenses</b>          | <b>278,982</b>                                  | <b>274,718</b>      | <b>571,672</b>          | <b>545,753</b>      |
| <b>Interest Expense, Net</b>                                 | <b>17,394</b>                                   | <b>12,107</b>       | <b>27,980</b>           | <b>24,825</b>       |
| <b>Income Before Income Taxes</b>                            | <b>60,350</b>                                   | <b>80,913</b>       | <b>160,663</b>          | <b>181,062</b>      |
| <b>Provision for Income Taxes</b>                            | <b>18,624</b>                                   | <b>26,058</b>       | <b>49,420</b>           | <b>57,939</b>       |
| <b>Net Income</b>  | <b>\$ 41,726</b>                                | <b>\$ 54,855</b>    | <b>\$ 111,243</b>       | <b>\$ 123,123</b>   |
| <b>Average Number of Shares of Common Stock Outstanding:</b> |   |                     |                         |                     |
| <b>Basic</b>   | <b>127,090</b>                                  | <b>120,057</b>      | <b>126,158</b>          | <b>120,027</b>      |
| <b>Diluted</b>   | <b>128,137</b>                                  | <b>130,608</b>      | <b>129,197</b>          | <b>130,474</b>      |
| <b>Basic Earnings per Share of Common Stock</b>              | <b>\$ 0.33</b>                                  | <b>\$ 0.46</b>      | <b>\$ 0.88</b>          | <b>\$ 1.03</b>      |
| <b>Diluted Earnings per Share of Common Stock</b>            | <b>\$ 0.33</b>                                  | <b>\$ 0.43</b>      | <b>\$ 0.86</b>          | <b>\$ 0.96</b>      |
| <b>Cash Dividends Declared per Share of Common Stock</b>     | <b>\$ 0.200</b>                                 | <b>\$ 0.190</b>     | <b>\$ 0.390</b>         | <b>\$ 0.365</b>     |

The accompanying notes to consolidated financial statements are an integral part of these statements.

**Table of Contents****RPM INTERNATIONAL INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS**

|  | <b>Six Months Ended<br/>November 30,</b> |             |
|--|--|-------------|
|  | <b>2008</b>                              | <b>2007</b> |
|  | <b>(Unaudited)</b>                       |             |
|  | <b>(In thousands)</b>                    |             |
| <b>Cash Flows From Operating Activities:</b>   |  |             |
| Net income   | \$ 111,243                               | \$ 123,123  |
| Adjustments to reconcile net income to net cash provided by operating activities:        |  |             |
| Depreciation   | 32,175                                   | 30,962      |
| Amortization   | 11,254                                   | 10,813      |
| Deferred income taxes  | 5,034                                    | 20,294      |
| Earnings of unconsolidated affiliates  | (931)                                    | (606)       |
| Changes in assets and liabilities, net of effect from purchases and sales of businesses: |  |             |
| Decrease in receivables  | 212,078                                  | 120,336     |
| (Increase) in inventory  | (15,607)                                 | (29,130)    |
| (Increase) decrease in prepaid expenses and other current and long-term assets           | 18,138                                   | (4,648)     |
| (Decrease) in accounts payable   | (130,500)                                | (85,437)    |
| (Decrease) in accrued compensation and benefits  | (48,776)                                 | (32,304)    |
| Increase (decrease) in accrued loss reserves   | 1,693                                    | (6,692)     |
| (Decrease) in other accrued liabilities  | (37,279)                                 | (4,278)     |
| Payments made for asbestos-related claims  | (32,436)                                 | (48,873)    |
| Other  | (22,038)                                 | 10,531      |
| Cash From Operating Activities   | 104,048                                  | 104,091     |
| <b>Cash Flows From Investing Activities:</b>   |  |             |
| Capital expenditures   | (24,887)                                 | (17,477)    |
| Acquisition of businesses, net of cash acquired  | (3,733)                                  | (9,291)     |
| Purchase of marketable securities  | (69,133)                                 | (43,731)    |
| Proceeds from sales of marketable securities   | 63,612                                   | 41,103      |
| Proceeds from the sales of assets or businesses  |  | 44,800      |
| Other  | 3,296                                    | (338)       |
| Cash From (Used For) Investing Activities  | (30,845)                                 | 15,066      |
| <b>Cash Flows From Financing Activities:</b>   |  |             |
| Additions to long-term and short-term debt   | 87,209                                   | 5,727       |
| Reductions of long-term and short-term debt  | (49,576)                                 | (58,838)    |
| Cash dividends   | (50,470)                                 | (44,328)    |
| Repurchase of stock  | (45,184)                                 | (5,730)     |
| Exercise of stock options, including tax benefit   | 1,690                                    | 5,239       |

|   |            |            |
|---|------------|------------|
| Cash (Used For) Financing Activities                                      | (56,331)   | (97,930)   |
| <b>Effect of Exchange Rate Changes on Cash and Short-Term Investments</b> | (42,834)   | 10,837     |
| <b>Net Change in Cash and Short-Term Investments</b>                      | (25,962)   | 32,064     |
| <b>Cash and Short-Term Investments at Beginning of Period</b>             | 231,251    | 159,016    |
| <b>Cash and Short-Term Investments at End of Period</b>                   | \$ 205,289 | \$ 191,080 |

The accompanying notes to consolidated financial statements are an integral part of these statements.

Table of Contents**RPM INTERNATIONAL INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****NOVEMBER 30, 2008****(Unaudited)****NOTE A BASIS OF PRESENTATION**

The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and notes required by generally accepted accounting principles ( GAAP ) in the U.S. for complete financial statements. In our opinion, all adjustments (consisting of normal, recurring accruals) considered necessary for a fair presentation have been included for the three and six month periods ended November 30, 2008 and 2007. For further information, refer to the Consolidated Financial Statements and Notes included in our Annual Report on Form 10-K for the year ended May 31, 2008.

Our business is dependent on external weather factors. Historically, we have experienced strong sales and net income in our first, second and fourth fiscal quarters comprising the three month periods ending August 31, November 30 and May 31, respectively, with weaker performance in our third fiscal quarter (December through February).

Certain reclassifications have been made to prior year amounts to conform to the current year presentation.

**NOTE B MARKETABLE SECURITIES**

The following tables summarize marketable securities held at November 30, 2008 and May 31, 2008 by asset type:

|                                    | Available-For-Sale Securities |                     |                      | Estimated<br>Fair Value<br>(Net<br>Carrying<br>Amount) |
|------------------------------------|-------------------------------|---------------------|----------------------|--|
|                                    |                               | Gross               | Gross                |  |
| November 30, 2008                  | Amortized<br>Cost             | Unrealized<br>Gains | Unrealized<br>Losses |  |
|                                    | (In thousands)                |                     |                      |  |
| Equity securities:                 |                               |                     |                      |  |
| Stocks                             | \$ 41,176                     | \$ 359              | \$ (15,875)          | \$ 25,660  |
| Mutual funds                       | 23,532                        |                     | (7,310)              | 16,222   |
| Total equity securities            | 64,708                        | 359                 | (23,185)             | 41,882   |
| Fixed maturity:                    |                               |                     |                      |  |
| U.S. treasury and other government | 10,318                        | 533                 | (31)                 | 10,820   |
| Corporate                          | 17,147                        | 361                 | (391)                | 17,117   |
| Total fixed maturity securities    | 27,465                        | 894                 | (422)                | 27,937   |
| Total                              | \$ 92,173                     | \$ 1,253            | \$ (23,607)          | \$ 69,819  |



Table of Contents**RPM INTERNATIONAL INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

| May 31, 2008                       | Available-For-Sale Securities |                     |                      | Estimated<br>Fair Value<br>(Net<br>Carrying<br>Amount) |
|------------------------------------|-------------------------------|---------------------|----------------------|--|
|                                    | Amortized<br>Cost             | Gross               | Gross                |  |
|                                    |                               | Unrealized<br>Gains | Unrealized<br>Losses |  |
|                                    |                               | (In thousands)      |                      |  |
| Equity securities:                 |                               |                     |                      |  |
| Stocks                             | \$ 40,274                     | \$ 18,500           | \$ (1,034)           | \$ 57,740  |
| Mutual funds                       | 18,401                        | 2,020               | (418)                | 20,003   |
| Total equity securities            | 58,675                        | 20,520              | (1,452)              | 77,743   |
| Fixed maturity:                    |                               |                     |                      |  |
| U.S. treasury and other government | 19,934                        | 394                 | (95)                 | 20,233   |
| Corporate                          | 12,480                        | 144                 | (200)                | 12,424   |
| Total fixed maturity securities    | 32,414                        | 538                 | (295)                | 32,657   |
| Total                              | \$ 91,089                     | \$ 21,058           | \$ (1,747)           | \$ 110,400   |

Marketable securities, included in other current and long-term assets, are composed of available-for-sale securities and are reported at fair value, based on quoted market prices. Realized gains and losses on sales of investments are recognized in net income on the specific identification basis. Changes fair values of securities that are considered temporary, are recorded as unrealized gains and losses, net of applicable taxes, in accumulated other comprehensive income (loss) within stockholders' equity. Other-than-temporary declines in market value from original cost are reflected in operating income in the period in which the unrealized losses are deemed other than temporary. In order to determine whether an other-than-temporary decline in market value has occurred, the duration of the decline in value and our ability to hold the investment to recovery are considered in conjunction with an evaluation of the strength of the underlying collateral and the extent to which the investment's amortized cost or cost, as appropriate, exceeds its related market value.

Gross gains and losses realized on sales of investments were \$0.5 million and \$2.1 million, respectively for the quarter ended November 30, 2008. Gross gains and losses realized on sales of investments were \$1.6 million and \$0.4 million, respectively, for the quarter ended November 30, 2007. During the quarters ended November 30, 2008 and 2007, we recognized losses of \$2.6 million and \$57,000, respectively, for securities deemed to have other-than-temporary impairments. These amounts are included in net interest expense in the Consolidated Statements of Income.

Gross gains and losses realized on sales of investments were \$3.7 million and \$2.4 million, respectively, for the six months ended November 30, 2008. Gross gains and losses realized on sales of investments were \$2.7 million and \$0.6 million, respectively, for the six months ended November 30, 2007. During the six month periods ended November 30, 2008 and 2007, we recognized losses of \$3.4 million and \$0.1 million, respectively, for securities

deemed to have other-than-temporary impairments.

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Table of Contents**RPM INTERNATIONAL INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

Summarized below are the securities we held at November 30, 2008 and May 31, 2008 that were in an unrealized loss position included in accumulated other comprehensive income, aggregated by the length of time the investments had been in that position:

|  | <b>November 30, 2008</b> |                       | <b>May 31, 2008</b> |                   |
|--|--------------------------|-----------------------|---------------------|-------------------|
|  | <b>Fair</b>              | <b>Gross</b>          | <b>Fair</b>         | <b>Gross</b>      |
|  | <b>Value</b>             | <b>Unrealized</b>     | <b>Value</b>        | <b>Unrealized</b> |
|  |                          | <b>Losses</b>         |                     | <b>Losses</b>     |
|  |                          | <b>(In thousands)</b> |                     |                   |
| Total investments with unrealized losses                       | \$ 44,718                | \$ (23,607)           | \$ 25,785           | \$ (1,747)        |
| Unrealized losses with a loss position for less than 12 months | 39,502                   | (20,112)              | 24,730              | (1,635)           |
| Unrealized losses with a loss position for more than 12 months | 5,216                    | (3,495)               | 1,055               | (112)             |

Included in the figures above is our investment in Kemrock Industries, which has a fair value of \$12.2 million and an unrealized loss of \$8.3 million at November 30, 2008. At May 31, 2008, our investment in Kemrock Industries had a fair value of \$20.9 million, and was in an unrealized gain position. We have reviewed all of the securities included in the table above and have concluded that we have the ability and intent to hold these investments until their cost can be recovered, based upon the severity and duration of the decline. Therefore, we did not recognize any other-than-temporary impairment losses on these investments. Unrealized losses at November 30, 2008 were generally caused by the recent decline in valuations in the financial markets and the volatility in the global economy, specifically over the last few months of our recently completed second fiscal quarter. If general economic conditions were to continue to deteriorate, including continued uncertainties surrounding the volatility in financial markets and the viability of banks and other financial institutions, and if we were to experience continuing or significant additional unrealized losses within our portfolio of investments in marketable securities, we may recognize additional other-than-temporary impairment losses. Such potential losses could have a material impact on our results of operations. As such, we continue to closely evaluate the status of our investments and our ability and intent to hold these investments until their cost can be recovered.

The net carrying value of debt securities at November 30, 2008, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because the issuers of the securities may have the right to prepay obligations without prepayment penalties.

|                    | <b>Amortized</b>      | <b>Fair Value</b> |
|--------------------|-----------------------|-------------------|
|                    | <b>Cost</b>           |                   |
|                    | <b>(In thousands)</b> |                   |
| Due:               |                       |                   |
| Less than one year | \$ 1,348              | \$ 1,348          |

|                             |           |           |
|-----------------------------|-----------|-----------|
| One year through five years | 13,971    | 14,379    |
| Six years through ten years | 5,022     | 5,178     |
| After ten years             | 7,124     | 7,032     |
|                             | \$ 27,465 | \$ 27,937 |

#### **NOTE C FAIR VALUE MEASUREMENTS**

Effective June 1, 2008, we adopted Statement of Financial Accounting Standard No. 157 ( SFAS No. 157 ), Fair Value Measurements. SFAS No. 157 clarifies the definition of fair value, establishes a framework for measuring fair value based on the inputs used to measure fair value and expands the disclosures of fair value measurements. In accordance with Financial Accounting Standards Board Staff Position No. FAS 157-2, Effective Date of FASB Statement No. 157, we will defer the adoption of SFAS No. 157 for our nonfinancial assets and nonfinancial liabilities until June 1, 2009, which is not expected to have a material impact on our financial

Table of Contents**RPM INTERNATIONAL INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

statements. Our adoption of the portion of SFAS No. 157 relating to our financial assets and liabilities did not have a material impact on our financial statements.

SFAS No. 157 valuation techniques are based on observable and unobservable inputs. Observable inputs reflect readily obtainable data from independent sources, while unobservable inputs reflect management's market assumptions. The fair value hierarchy has three levels based on the reliability of the inputs used to determine fair value, as follows:

Level 1 Inputs Quoted prices for identical instruments in active markets.

Level 2 Inputs Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.

Level 3 Inputs Instruments with primarily unobservable value drivers.

The following table presents our assets and liabilities that are measured at fair value on a recurring basis and are categorized using the fair value hierarchy.

|                              | <b>Quoted Prices<br/>in<br/>Active<br/>Markets for<br/>Identical<br/>Assets<br/><br/>(Level 1)</b> |        | <b>Significant<br/>Other<br/>Observable<br/>Inputs<br/><br/>(Level 2)</b> | <b>Significant<br/>Unobservable<br/>Inputs<br/><br/>(Level 3)</b> | <b>Fair Value at<br/>November 30,<br/>2008</b> |
|------------------------------|--|--------|---|---|--|
|                              |  |        | <b>(In thousands)</b>   |   |  |
| Marketable securities        | \$   | 70,486 | \$  |   | \$ 70,486                                      |
| Derivatives, net (liability) |  |        |   | 7,509   | 7,509  |
| Total                        | \$   | 70,486 | \$  | 7,509   | \$ 77,995                                      |

**NOTE D INVENTORIES**

Inventories were composed of the following major classes:

**November 30,  
2008**      **May 31, 2008**  
**(In thousands)**

|                           |    |         |    |         |
|---------------------------|----|---------|----|---------|
| Raw material and supplies | \$ | 152,283 | \$ | 151,400 |
| Finished goods            |    | 340,958 |    | 324,749 |
| <b>Total Inventory</b>    | \$ | 493,241 | \$ | 476,149 |

Table of Contents**RPM INTERNATIONAL INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE E COMPREHENSIVE INCOME**

The following table illustrates the components of total comprehensive income for each of the three and six month periods ended November 30, 2008 and 2007:

|  | <b>Three Months Ended<br/>November 30,</b> |                   | <b>Six Months Ended<br/>November 30,</b> |                   |
|--|--|-------------------|--|-------------------|
|  | <b>2008</b>                                | <b>2007</b>       | <b>2008</b>                              | <b>2007</b>       |
|  | <b>(In thousands)</b>                      |                   |  |                   |
| Net income   | \$ 41,726                                  | \$ 54,855         | \$ 111,243                               | \$ 123,123        |
| Other Comprehensive Income:  |  |                   |  |                   |
| Foreign currency translation adjustments                                   | (125,465)                                  | 35,089            | (173,871)                                | 38,757            |
| Pension and other postretirement benefit liability adjustments, net of tax | 3,063                                      | 928               | 4,987                                    | (1,380)           |
| Unrealized gain (loss) on securities, net of tax                           | (16,840)                                   | 10,802            | (27,804)                                 | 9,660             |
| Derivatives income, net of tax   | 46   | 3,949             | 1,246                                    | 5,621             |
| <b>Total Comprehensive Income (Loss)</b>                                   | <b>\$ (97,470)</b>                         | <b>\$ 105,623</b> | <b>\$ (84,199)</b>                       | <b>\$ 175,781</b> |

**NOTE F CONTINGENCIES AND OTHER ACCRUED LOSSES***Asbestos-related Contingencies*

Certain of our wholly-owned subsidiaries, principally Bondex International, Inc. (collectively referred to as our subsidiaries), are defendants in various asbestos-related bodily injury lawsuits filed in various state courts with the vast majority of current claims pending in six states – Texas, Florida, Mississippi, Maryland, Illinois and Ohio. These cases generally seek unspecified damages for asbestos-related diseases based on alleged exposures to asbestos-containing products previously manufactured by our subsidiaries or others.

As of November 30, 2008, our subsidiaries had a total of 10,048 active asbestos cases compared to a total of 11,117 cases as of November 30, 2007. For the quarter ended November 30, 2008, our subsidiaries secured dismissals and/or settlements of 1,824 cases and made total payments of \$16.4 million, which included defense-related payments of \$6.1 million. For the comparable period ended November 30, 2007, dismissals and/or settlements covered 292 cases and total payments were \$26.1 million, which included defense-related payments of \$13.8 million. For the six months ended November 30, 2008, our subsidiaries secured dismissals and/or settlements of 2,025 cases and made total payments of \$32.4 million, which included defense-related payments of \$12.8 million. For the comparable period ended November 30, 2007, dismissals and/or settlements covered 657 cases and total payments were \$48.9 million, which included defense-related payments of \$22.6 million.

Of the 1,824 cases that were dismissed in the quarter ended November 30, 2008, 1,420 were non-malignancies or unknown disease cases that had been maintained on an inactive docket in Ohio and were administratively dismissed

by the Cuyahoga County Court of Common Pleas. These claims were dismissed without prejudice and may be re-filed should the claimants involved be able to demonstrate disease in accordance with medical criteria laws established in the state of Ohio.

During the prior fiscal year, our subsidiaries incurred higher year-over-year, defense-related payments as a result of implementing various changes to our management and defense of asbestos claims, including a transition to a new claims intake and database service provider. To facilitate that transition and other related changes, we incurred duplicate defense-related payments approximating \$3.0 million during last year's second fiscal quarter. The transition was completed during the quarter ended February 29, 2008.

Excluding defense-related payments, the average payment made to settle or dismiss a case approximated \$6,000 and \$42,000 for each of the quarters ended November 30, 2008 and 2007, respectively. As discussed above,

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**RPM INTERNATIONAL INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

there were approximately 1,420 non-malignancies or unknown disease cases that were administratively dismissed during the current fiscal quarter. Excluding those dismissed cases, the average payment made to settle or dismiss a case approximated \$25,000 for the quarter ended November 30, 2008. The amount and timing of dismissals and settlements can fluctuate significantly from period to period, resulting in volatility in the average cost to resolve a case in any given quarter or year. In addition, in some jurisdictions, cases may involve more than one individual claimant. As a result, settlement or dismissal payments made on a per case basis are not necessarily reflective of the payment amounts on a per claimant basis. For example, the amount paid to settle or dismiss a case can vary widely depending on a variety of factors, including the mix of malignancy and non-malignancy claimants, and the amount of defense expenditures incurred during the period.

Estimating the future cost of asbestos-related contingent liabilities was and continues to be subject to many uncertainties that may change over time, including (i) the ultimate number of claims filed; (ii) the amounts required to resolve both currently known and future unknown claims; (iii) the amount of insurance, if any, available to cover such claims, including the outcome of coverage litigation against our subsidiaries' third-party insurers; (iv) future earnings and cash flow of our subsidiaries; (v) the impact of bankruptcies of other companies whose share of liability may be imposed on our subsidiaries under certain state liability laws; (vi) the unpredictable aspects of the litigation process including a changing trial docket and the jurisdictions in which trials are scheduled; (vii) the outcome of any such trials including judgments or jury verdicts, as a result of our more aggressive defense posture, which includes taking selective cases to verdict; (viii) the lack of specific information in many cases concerning exposure to products for which one of our subsidiaries is responsible and the claimants' diseases; (ix) potential changes in applicable federal and/or state law; and (x) the potential impact of various proposed structured settlement transactions or subsidiary bankruptcies by other companies, some of which are the subject of federal appellate court review, the outcome of which could materially affect any future asbestos-related liability estimates.

In fiscal 2006, we retained Crawford & Winiarski (C&W), an independent, third-party consulting firm with expertise in the area of asbestos valuation work, to assist us in calculating an estimate of our liability for unasserted-potential-future-asbestos-related claims. The methodology used by C&W to project our liability for unasserted-potential-future-asbestos-related claims included C&W doing an analysis of: (a) widely accepted forecast of the population likely to have been exposed to asbestos; (b) epidemiological studies estimating the number of people likely to develop asbestos-related diseases; (c) historical rate at which mesothelioma incidences resulted in the payment of claims by us; (d) historical settlement averages to value the projected number of future compensable mesothelioma claims; (e) historical ratio of mesothelioma-related-indemnity payments to non-mesothelioma indemnity payments; and (f) historical defense costs and their relationship with total indemnity payments.

During fiscal 2006, we recorded a liability for asbestos claims in the amount of \$380.0 million, while paying out \$59.9 million for dismissals and/or settlements, which resulted in our accrued liability balance moving from \$101.2 million at May 31, 2005 to \$421.3 million at May 31, 2006. This increase was based largely upon C&W's analysis of our total estimated liability for unasserted-potential-future-asbestos-related claims through May 31, 2016. This amount was also calculated on a pre-tax basis and was not discounted for the time value of money. In light of the uncertainties inherent in making long-term projections, we determined at that time that a ten-year period was the most reasonable time period over which reasonably accurate estimates might still be made for projecting asbestos liabilities and defense costs and, accordingly, our accrual did not include asbestos liabilities for any period beyond ten years.

During the fiscal year ended May 31, 2008, we reviewed and evaluated our ten-year asbestos liability established as of May 31, 2006. As part of that review and evaluation process, the credibility of epidemiological studies of our mesothelioma claims, first introduced to management by C&W some two-and-one-half years ago, was validated. At the core of our evaluation process, and the basis of C&W's actuarial work on behalf of Bondex, is the *Nicholson Study*. The *Nicholson Study* is the most widely recognized reference in bankruptcy trust valuations, global settlement negotiations and the Congressional Budget Offices' work done on the proposed FAIR Act in 2006. Based on our ongoing comparison of the *Nicholson Study* projections and Bondex's specific actual experience,

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**RPM INTERNATIONAL INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

which continues to bear an extremely close correlation to the study's projections, we decided to extend our asbestos liability projection out to twenty years. C&W assisted us in calculating an estimate of our liability for unasserted-potential-future-asbestos-related claims out to that twenty-year period.

C&W has projected that the cost of extending the asbestos liability to twenty years, coupled with an updated evaluation of our current known claims to reflect our most recent actual experience, would be \$288.1 million. Therefore, we added \$288.1 million to our existing asbestos liability, which brought our total asbestos-related balance sheet liabilities at May 31, 2008 to \$559.7 million. Of that total, \$65.0 million was estimated to be the short-term liability due in fiscal 2009, with the remaining \$494.7 million balance reflected as a long-term liability. The material components of the accruals are: (i) the gross number of open malignancy claims (principally mesothelioma claims) as these claims have the most significant impact on our asbestos settlement costs; (ii) historical and current settlement costs and dismissal rates by various categories; (iii) analysis of the jurisdiction and governing laws of the states in which these claims are pending; (iv) outside defense counsel's opinions and recommendations with respect to the merits of such claims; and (v) analysis of projected liabilities for unasserted potential future claims.

In determining the amount of our asbestos liability, we relied on assumptions that are based on currently known facts and projection models. Our actual expenses could be significantly higher or lower than those recorded if assumptions used in our calculations vary significantly from actual results. Key variables in these assumptions include the period of exposure to asbestos claims, the number and type of new claims to be filed each year, the rate at which mesothelioma incidences result in compensable claims against us, the average cost of disposing of each such new claim, the dismissal rates each year and the related annual defense costs. Furthermore, predictions with respect to these variables are subject to greater uncertainty as the projection period lengthens. A significant upward or downward trend in the number of claims filed, depending on the nature of the alleged injury, the jurisdiction where filed, the average cost of resolving each such claim and the quality of the product identification, could change our estimated liability, as could any substantial adverse verdict at trial. A federal legislative solution, further state tort reform or a structured-settlement transaction could also change the estimated liability.

Subject to the foregoing variables, and based on currently available data, we believe that our current asbestos liability is sufficient to cover asbestos-related expenses for our known pending and unasserted-potential-future-asbestos-related claims through 2028. However, given the uncertainties associated with projecting matters into the future and numerous other factors outside of our control, we believe that it is reasonably possible we may incur additional material asbestos liabilities in periods before 2028. Due to the uncertainty inherent in the process undertaken to estimate our losses, we are unable at the present time to estimate an additional range of loss in excess of our existing accruals. While it is reasonably possible that such excess liabilities could be material to operating results in any given quarter or year, we do not believe that it is reasonably possible that such excess liabilities would have a material adverse effect on our long-term results of operations, liquidity or consolidated financial position.

During fiscal 2004, certain of our subsidiaries' third-party insurers claimed exhaustion of coverage. Certain of our subsidiaries have filed a complaint for declaratory judgment, breach of contract and bad faith against these third-party insurers, challenging their assertion that their policies covering asbestos-related claims have been exhausted. The coverage litigation involves, among other matters, insurance coverage for claims arising out of alleged exposure to asbestos containing products manufactured by the previous owner of the Bondex tradename before March 1, 1966. On March 1, 1966, Republic Powdered Metals Inc. (as it was known then), purchased the assets and assumed the

liabilities of the previous owner of the Bondex tradename. That previous owner subsequently dissolved and was never a subsidiary of Republic Powdered Metals, Bondex, RPM, Inc. or the Company. Because of the earlier assumption of liabilities, however, Bondex has historically responded, and must continue to respond, to lawsuits alleging exposure to these asbestos-containing products. We discovered that the defendant insurance companies in the coverage litigation had wrongfully used cases alleging exposure to these pre-1966 products to erode their aggregate limits. This conduct, apparently known by the insurance industry based on discovery conducted to date, was in breach of the insurers' policy language. Two of the defendant insurers have filed counterclaims seeking to recoup certain monies should the plaintiffs prevail on their claims.

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During the second fiscal quarter ended November 30, 2006, plaintiffs reached a settlement of \$15.0 million, the terms of which are confidential by agreement of the parties, with one of the defendant insurers. The settling defendant was dismissed from the case.

In 2007, plaintiffs had filed motions for partial summary judgment against the defendants and defendants had filed motions for summary judgment against plaintiffs. In addition, plaintiffs had filed a motion to dismiss the counterclaim filed by one of the defendants. On December 1, 2008, the court decided the pending motions for summary judgment and dismissal. The court denied the plaintiffs' motions for partial summary judgment and granted the defendants' motions for summary judgment against plaintiffs on a narrow ground. The court also granted the plaintiffs' motion to dismiss one defendant's amended counterclaim. In light of its summary judgment rulings, the court entered judgment as a matter of law on all remaining claims and counterclaims, including the counterclaim filed by another defendant, and dismissed the action. The court also dismissed certain remaining motions as moot. Because the scope of the court's order is unclear, plaintiffs and one defendant have filed motions with the court seeking clarification and amendment of the court's memorandum and order. Plaintiffs intend to file an appeal to the United States Sixth Circuit Court of Appeals and will continue to aggressively pursue their claims on appeal.

We are unable at the present time to predict the timing or ultimate outcome of this insurance coverage litigation or whether there will be any further settlements. Consequently, we are unable to predict whether, or to what extent, any additional insurance may be available to cover a portion of our subsidiaries' asbestos liabilities. We have not included any potential benefits from this litigation in calculating our current asbestos liability. Our wholly-owned captive insurance companies have not provided any insurance or reinsurance coverage for any of our subsidiaries' asbestos-related claims.

The following table illustrates the movement of current and long-term asbestos-related liabilities through November 30, 2008:

**Asbestos Liability Movement  
(Current and Long-Term)**

|                                    | <b>Balance at<br/>Beginning of<br/>Period</b> | <b>Additions to<br/>Asbestos<br/>Charge<br/>(In<br/>thousands)</b> | <b>Deductions*</b> | <b>Balance at<br/>End of<br/>Period</b> |
|------------------------------------|---|--|--------------------|---|
| Six Months Ended November 30, 2008 | \$ 559,745                                    |  | \$ 32,436          | \$ 527,309                              |
| Year Ended May 31, 2008            | 354,268                                       | \$ 288,100   | 82,623             | 559,745                                 |
| Year Ended May 31, 2007            | 421,285                                       |  | 67,017             | 354,268                                 |

\* Deductions include payments for defense-related costs and amounts paid to settle claims.

***Other Contingencies***

We provide, through our wholly-owned insurance subsidiaries, certain insurance coverage, primarily product liability, to our other subsidiaries. Excess coverage is provided by third-party insurers. Our reserves provide for these potential losses as well as other uninsured claims. As of November 30, 2008, the current portion of these reserves amounted to \$59.4 million as compared with \$56.5 million at May 31, 2008, while the total long-term reserves of \$7.2 million at November 30, 2008 compare with \$8.5 million at May 31, 2008. Product warranty expense is recorded within selling, general and administrative expense. We also offer a warranty program for our roofing systems and have established a product warranty liability. We review this liability for adequacy on a quarterly basis and adjust it as necessary. The primary factors that could affect this liability may include changes in the historical system performance rate as well as the costs of replacement. Provision for estimated warranty costs is recorded at the time of sale and periodically adjusted, as required, to reflect actual experience.

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In addition, like other companies participating in similar lines of business, some of our subsidiaries are involved in several proceedings relating to environmental matters. It is our policy to accrue remediation costs when it is probable that such efforts will be required and the related costs can be reasonably estimated. These liabilities are undiscounted.

**NOTE G PENSION AND POSTRETIREMENT HEALTH CARE BENEFITS**

We account for our pension plans and postretirement benefit plans in accordance with the provisions of SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*. We offer defined benefit pension plans, defined contribution pension plans, as well as several unfunded health care benefit plans primarily for certain of our retired employees. The following tables provide the retirement-related benefit plans' impact on income before income taxes for the three and six month periods ended November 30, 2008 and 2007:

| <b>Pension Benefits</b>          | <b>U.S. Plans</b>       |                         | <b>Non-U.S. Plans</b>   |                         |
|----------------------------------|-------------------------|-------------------------|-------------------------|-------------------------|
|                                  | <b>Six Months Ended</b> | <b>Six Months Ended</b> | <b>Six Months Ended</b> | <b>Six Months Ended</b> |
|                                  | <b>November 30,</b>     | <b>November 30,</b>     | <b>November 30,</b>     | <b>November 30,</b>     |
|                                  | <b>2008</b>             | <b>2007</b>             | <b>2008</b>             | <b>2007</b>             |
|                                  | <b>(In thousands)</b>   |                         |                         |                         |
| Service cost                     | \$ 7,360                | \$ 7,120                | \$ 1,519                | \$ 1,734                |
| Interest cost                    | 5,954                   | 5,148                   | 3,830                   | 3,268                   |
| Expected return on plan assets   | (6,446)                 | (6,660)                 | (3,693)                 | (3,357)                 |
| Amortization of:                 |                         |                         |                         |                         |
| Prior service cost               | 171                     | 120                     | 2                       | 13                      |
| Net actuarial losses recognized  | 1,326                   | 707                     | 622                     | 763                     |
| <b>Net Periodic Benefit Cost</b> | <b>\$ 8,365</b>         | <b>\$ 6,435</b>         | <b>\$ 2,280</b>         | <b>\$ 2,421</b>         |

| <b>Postretirement Benefits</b>          | <b>U.S. Plans</b>     |                     | <b>Non-U.S. Plans</b> |                     |
|---|-----------------------|---------------------|-----------------------|---------------------|
|   | <b>Six Months</b>     | <b>Six Months</b>   | <b>Six Months</b>     | <b>Six Months</b>   |
|   | <b>Ended</b>          | <b>Ended</b>        | <b>Ended</b>          | <b>Ended</b>        |
|   | <b>November 30,</b>   | <b>November 30,</b> | <b>November 30,</b>   | <b>November 30,</b> |
|   | <b>2008</b>           | <b>2007</b>         | <b>2008</b>           | <b>2007</b>         |
|   | <b>(In thousands)</b> |                     |                       |                     |
| Service cost                            | \$                    | \$                  | \$ 196                | \$ 247              |
| Interest cost                           | 216                   | 261                 | 378                   | 337                 |
| Prior service cost                      | (14)                  | (14)                |                       |                     |
| Net actuarial (gains) losses recognized | (48)                  |                     |                       | 44                  |
| <b>Net Periodic Benefit Cost</b>        | <b>\$ 154</b>         | <b>\$ 247</b>       | <b>\$ 574</b>         | <b>\$ 628</b>       |



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| <b>Pension Benefits</b>          | <b>U.S. Plans<br/>Quarter Ended<br/>November 30,</b> |                 | <b>Non-U.S. Plans<br/>Quarter Ended<br/>November 30,</b> |                 |
|----------------------------------|--|-----------------|--|-----------------|
|                                  | <b>2008</b>  | <b>2007</b>     | <b>2008</b>  | <b>2007</b>     |
|                                  | <b>(In thousands)</b>                                |                 |  |                 |
| Service cost                     | \$ 3,654   | \$ 3,560        | \$ 759   | \$ 867          |
| Interest cost                    | 3,026  | 2,574           | 1,915  | 1,634           |
| Expected return on plan assets   | (3,217)  | (3,330)         | (1,846)  | (1,678)         |
| Amortization of:                 |  |                 |  |                 |
| Prior service cost               | 86   | 60              | 1  | 7               |
| Net actuarial losses recognized  | 767  | 353             | 311  | 382             |
| <b>Net Periodic Benefit Cost</b> | <b>\$ 4,316</b>                                      | <b>\$ 3,217</b> | <b>\$ 1,140</b>  | <b>\$ 1,212</b> |

| <b>Postretirement Benefits</b>          | <b>U.S. Plans<br/>Quarter Ended<br/>November 30,</b> |               | <b>Non-U.S. Plans<br/>Quarter Ended<br/>November 30,</b> |               |
|---|--|---------------|--|---------------|
|   | <b>2008</b>  | <b>2007</b>   | <b>2008</b>  | <b>2007</b>   |
|   | <b>(In thousands)</b>                                |               |  |               |
| Service cost                            | \$   | \$            | \$ 98  | \$ 124        |
| Interest cost                           | 108  | 131           | 189  | 169           |
| Prior service cost                      | (7)  | (7)           |  |               |
| Net actuarial (gains) losses recognized | (24)   |               |  | 22            |
| <b>Net Periodic Benefit Cost</b>        | <b>\$ 77</b>   | <b>\$ 124</b> | <b>\$ 287</b>  | <b>\$ 315</b> |

We previously disclosed in our financial statements for the fiscal year ended May 31, 2008 that we expected to contribute approximately \$10.3 million to the Retirement Plans in the U.S. and approximately \$7.5 million to plans outside the U.S. during the current fiscal year. As of November 30, 2008, we have updated our expected contributions to the Retirement Plans in the U.S. to be \$10.2 million. Additionally, the figures included in the tables above reflect a change in expense as a result of our recently updated actuarial data. The increase in the U.S. pension expense that was not included in our first quarter figures have been included in the second quarter expense.

We have determined that our postretirement medical plan provides prescription drug benefits that will qualify for the federal subsidy provided by the Medicare Prescription Drug, Improvement and Modernization Act of 2003. For all groups of retirees, we have assumed that the subsidy will continue indefinitely.

As previously disclosed, we adopted the provisions of SFAS No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106 and 132(R) beginning with our fiscal year ended May 31, 2008, and transitioned from a measurement date of February 28 to May 31.

**NOTE H EARNINGS PER SHARE**

Our basic earnings per share calculation is based on the weighted-average number of shares of common stock outstanding. Our diluted earnings per share calculation is based on the weighted-average number of shares of common stock outstanding adjusted for the number of additional shares that would have been outstanding had all potentially dilutive common shares been issued. Potentially dilutive shares of common stock include stock options, nonvested share awards and shares issuable under our employee stock purchase plan, as well as shares of common stock that would have been issued pursuant to the assumed conversion of our convertible notes. Since the potentially dilutive shares related to the convertible notes are included in the calculation of diluted earnings per share, the

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related interest expense, net of tax, is added back to net earnings, as this interest would not have been paid if the convertible notes had been converted to common stock. Nonvested market-based stock awards and nonvested performance-based awards are included in the average diluted shares outstanding each period if established market or performance criteria have been met at the end of the respective periods.

|  | Quarter Ended<br>November 30, |           | Six Months Ended<br>November 30, |            |
|--|-------------------------------|-----------|----------------------------------|------------|
|  | 2008                          | 2007      | 2008                             | 2007       |
| (In thousands, except per share amounts)                                 |                               |           |                                  |            |
| <b>Shares Outstanding</b>  |                               |           |                                  |            |
| Weighted-average common shares outstanding                               | 127,090                       | 120,057   | 126,158                          | 120,027    |
| Net issuable common share equivalents                                    | 1,047                         | 2,518     | 1,363                            | 2,414      |
| Additional shares issuable assuming conversion of convertible securities |                               | 8,033     | 1,676                            | 8,033      |
| Total shares for diluted earnings per share                              | 128,137                       | 130,608   | 129,197                          | 130,474    |
| <b>Net Income</b>  |                               |           |                                  |            |
| Net income, basic  | \$ 41,726                     | \$ 54,855 | \$ 111,243                       | \$ 123,123 |
| Add: Income effect of convertible securities                             |                               | 771       | 280                              | 1,542      |
| Net income, diluted  | \$ 41,726                     | \$ 55,626 | \$ 111,523                       | \$ 124,665 |
| <b>Earnings Per Share</b>  |                               |           |                                  |            |
| Basic Earnings Per Share of Common Stock                                 | \$ 0.33                       | \$ 0.46   | \$ 0.88                          | \$ 1.03    |
| Diluted Earnings Per Share of Common Stock                               | \$ 0.33                       | \$ 0.43   | \$ 0.86                          | \$ 0.96    |

**NOTE I INCOME TAXES**

The effective income tax rate was 30.9% for the three months ended November 30, 2008 compared to an effective income tax rate of 32.2% for the three months ended November 30, 2007.

For the three months ended November 30, 2008 and, to a lesser extent for the three months ended November 30, 2007, the effective tax rate differed from the federal statutory rate principally due to decreases in taxes as a result of the impact of certain foreign operations on our U.S. taxes and the effect of lower tax rates in certain of our foreign jurisdictions. The decreases in the effective tax rates were partially offset by provisions for valuation allowances associated with losses incurred by certain of our foreign businesses, state and local income taxes and other non-deductible business operating expenses.

The effective income tax rate was 30.8% for the six months ended November 30, 2008 compared to an effective income tax rate of 32.0% for the six months ended November 30, 2007.

For the six months ended November 30, 2008 and, to a lesser extent for the six months ended November 30, 2007, the effective tax rate differed from the federal statutory rate principally as a result of the impact of certain foreign operations on our U.S. taxes and the effect of lower tax rates in certain of our foreign jurisdictions. The decreases in the effective tax rates were partially offset by valuation allowances associated with losses incurred by certain of our foreign businesses, state and local income taxes and other non-deductible business operating expenses.

As of November 30, 2008, we had unrecognized tax benefits of approximately \$3.2 million, of which approximately \$2.4 million would impact the effective tax rate, if recognized. We recognize interest and penalties related to unrecognized tax benefits in income tax expense. At November 30, 2008, the accrual for interest and penalties totaled approximately \$1.3 million.

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**RPM INTERNATIONAL INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

We file income tax returns in the U.S. and various state, local and foreign jurisdictions. As of November 30, 2008, we are subject to U.S. federal income tax examinations for the fiscal years 2005 through 2008. In addition, with limited exceptions, we are subject to various state and local or non-U.S. income tax examinations by tax authorities for the fiscal years 2002 through 2008. We do not anticipate any significant changes to the total unrecognized tax benefits within the next 12 months.

**NOTE J SEGMENT INFORMATION**

We operate a portfolio of businesses and product lines that manufacture and sell a variety of specialty paints, protective coatings and roofing systems, sealants and adhesives. We manage our portfolio by organizing our businesses and product lines into two reportable segments: the industrial reportable segment and the consumer reportable segment. Within each reportable segment, we aggregate three operating segments that consist of individual groups of companies and product lines, which generally address common markets, share similar economic characteristics, utilize similar technologies and can share manufacturing or distribution capabilities. Our six operating segments represent components of our business for which separate financial information is available that is utilized on a regular basis by our chief executive officer in determining how to allocate the assets of the Company and evaluate performance. These six operating segments are each managed by an operating segment manager, who is responsible for the day-to-day operating decisions and performance evaluation of the operating segment's underlying businesses.

Our industrial reportable segment products are sold throughout North America and also account for the majority of our international sales. Our industrial product lines are sold directly to contractors, distributors and end-users, such as industrial manufacturing facilities, public institutions and other commercial customers. This reportable segment comprises three separate operating segments – our Tremco Group, StonCor Group, and RPM II/Industrial Group. Products and services within this reportable segment include construction chemicals, roofing systems, weatherproofing and other sealants, flooring and specialty chemicals.

Our consumer reportable segment manufactures and markets professional use and do-it-yourself (DIY) products for a variety of mainly consumer applications, including home improvement and personal leisure activities. Our consumer segment's major manufacturing and distribution operations are located primarily in North America, along with a few locations in Europe. Consumer segment products are sold directly to mass merchandisers, home improvement centers, hardware stores, paint stores, craft shops and to other smaller customers through distributors. This reportable segment comprises three operating segments – our DAP Group, Rust-Oleum/Zinsser Group, and RPM II/Consumer Group. Products within this reportable segment include specialty, hobby and professional paints; caulks; adhesives; silicone sealants; wood stains and specialty confectionary coatings and films.

In addition to our two reportable segments, there is a category of certain business activities and expenses, referred to as corporate/other, that does not constitute an operating segment. This category includes our corporate headquarters and related administrative expenses, results of our captive insurance companies, gains or losses on the sales of certain assets and other expenses not directly associated with either reportable segment. Assets related to the corporate/other category consist primarily of investments, prepaid expenses, deferred pension assets, and headquarters' property and equipment. These corporate and other assets and expenses reconcile reportable segment data to total consolidated income before income taxes and identifiable assets. Our comparative three and six month



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results for the periods ended November 30, 2008 and 2007, and identifiable assets as of November 30, 2008 and May 31, 2008 are presented in segment detail in the following table.

|  | <b>Three Months Ended<br/>November 30,<br/>2008</b> |                   | <b>Six Months Ended<br/>November 30,<br/>2008</b> |                     |
|--|---|-------------------|---|---------------------|
|  | <b>2007</b>   | <b>2007</b>       | <b>2008</b>                                       | <b>2007</b>         |
|  | <b>(In thousands)</b>                               |                   |   |                     |
| <b>Net Sales</b>                         |   |                   |   |                     |
| Industrial Segment                       | \$ 625,578  | \$ 605,846        | \$ 1,323,160                                      | \$ 1,214,446        |
| Consumer Segment                         | 264,387   | 299,862           | 552,270   | 621,601             |
| <b>Consolidated</b>                      | <b>\$ 889,965</b>                                   | <b>\$ 905,708</b> | <b>\$ 1,875,430</b>                               | <b>\$ 1,836,047</b> |
| <b>Gross Profit</b>                      |   |                   |   |                     |
| Industrial Segment                       | \$ 264,409  | \$ 254,315        | \$ 556,184  | \$ 509,859          |
| Consumer Segment                         | 92,317  | 113,423           | 204,131   | 241,781             |
| <b>Consolidated</b>                      | <b>\$ 356,726</b>                                   | <b>\$ 367,738</b> | <b>\$ 760,315</b>                                 | <b>\$ 751,640</b>   |
| <b>Income (Loss) Before Income Taxes</b> |   |                   |   |                     |
| Industrial Segment                       | \$ 70,958   | \$ 73,058         | \$ 162,470  | \$ 152,710          |
| Consumer Segment                         | 14,806  | 29,819            | 48,071  | 72,670              |
| Corporate/Other                          | (25,414)  | (21,964)          | (49,878)  | (44,318)            |
| <b>Consolidated</b>                      | <b>\$ 60,350</b>                                    | <b>\$ 80,913</b>  | <b>\$ 160,663</b>                                 | <b>\$ 181,062</b>   |
| <b>Identifiable Assets</b>               |   |                   | <b>November 30, 2008</b>                          | <b>May 31, 2008</b> |
| Industrial Segment                       |   |                   | \$ 1,900,787                                      | \$ 2,130,532        |
| Consumer Segment                         |   |                   | 1,180,649   | 1,342,572           |
| Corporate/Other                          |   |                   | 271,766   | 290,463             |
| <b>Consolidated</b>                      |   |                   | <b>\$ 3,353,202</b>                               | <b>\$ 3,763,567</b> |

**NOTE K STOCK REPURCHASE PROGRAM**

On January 8, 2008, we announced our authorization of a stock repurchase program under which we may repurchase shares of RPM International Inc. common stock at management's discretion for general corporate purposes. Our current intent is to limit our repurchases only to amounts required to offset dilution created by stock issued in

connection with our equity-based compensation plans, or approximately one to two million shares per year. As a result of this authorization, we may repurchase shares from time to time in the open market or in private transactions at various times and in amounts and for prices that our management deems appropriate, subject to insider trading rules and other securities law restrictions. The timing of our purchases will depend upon prevailing market conditions, alternative uses of capital and other factors. We may limit or terminate the repurchase program at any time. During the six month period ended November 30, 2008, we repurchased approximately 2.4 million shares of our common stock at a cost of approximately \$43.4 million under this program.

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**RPM INTERNATIONAL INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**NOTE L CONVERTIBLE NOTES**

As previously reported, during our first fiscal quarter ended August 31, 2008, our Senior Convertible Notes (the Convertible Notes ) due May 13, 2033 became eligible for conversion based upon the price of RPM International Inc. common stock. Subsequent to this event, on June 13, 2008, we called for the redemption of all of our outstanding Convertible Notes on the effective date of July 14, 2008 (the Redemption Date ). Prior to the Redemption Date, virtually all of the holders had already converted their Convertible Notes into 8,030,455 shares of RPM International Inc. common stock, or 27.0517 shares of common stock for each \$1,000 Face Value Convertible Note they held. Any fractional shares from the conversion were paid in cash.

**NOTE M NEW ACCOUNTING STANDARDS**

In December 2007, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standards ( SFAS ) No. 141(R), Business Combinations, and SFAS No. 160, Accounting and Reporting of Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51. SFAS No. 141(R) and SFAS No. 160 are required to be adopted simultaneously and are effective for our fiscal year ending May 31, 2010. Under SFAS No. 141(R), upon initially obtaining control of another entity or business, an acquirer will recognize 100% of the fair values of assets acquired, including goodwill, and liabilities assumed, with limited exceptions, even if the acquirer has not acquired 100% of the target. Also, under SFAS No. 141(R), transaction costs will no longer be considered part of the fair value of an acquisition, and will be expensed as incurred. We are currently evaluating the impact that the adoption of this statement will have on our financial statements.

SFAS No. 160 improves the relevance, comparability and transparency of financial information provided to investors by requiring all entities to report noncontrolling (minority) interests in subsidiaries in the same way. Additionally, SFAS No. 160 eliminates the diversity that currently exists in accounting for transactions between an entity and noncontrolling interests by requiring they be treated as equity transactions. SFAS No. 160 is effective for our fiscal year ending May 31, 2010. We are currently evaluating the impact that the adoption of this statement will have on our financial statements.

In March 2008, the FASB issued SFAS No. 161 ( SFAS No. 161 ), Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133. SFAS No. 161 requires enhanced disclosures about an entity's derivative and hedging activities, including (i) how and why an entity uses derivative instruments, (ii) how derivative instruments and related hedged items are accounted for under SFAS 133, and (iii) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. SFAS No. 161 is effective for our third fiscal quarter ending February 28, 2009. As the provisions of SFAS No. 161 relate only to enhanced disclosures, this standard will have no impact on our financial position, results of operations or cash flows.

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

**CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

Our Consolidated Financial Statements include the accounts of RPM International Inc. and its majority-owned subsidiaries. Preparation of our financial statements requires the use of estimates and assumptions that affect the reported amounts of our assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. We continually evaluate these estimates, including those related to our asbestos liability; allowances for doubtful accounts; inventories; allowances for recoverable taxes; useful lives of property, plant and equipment; goodwill and other intangible assets; environmental and other contingent liabilities; income tax valuation allowances; pension plans; and the fair value of financial instruments. We base our estimates on historical experience, our most recent facts, and other assumptions that we believe to be reasonable under the circumstances. These estimates form the basis for making judgments about the carrying values of our assets and liabilities. Actual results, which are shaped by actual market conditions, including legal settlements, may differ materially from our estimates.

We have identified below the accounting policies and estimates that are the most critical to our financial statements.

***Revenue Recognition***

Revenues are recognized when realized or realizable, and when earned. In general, this is when title and risk of loss pass to the customer. Further, revenues are realizable when we have persuasive evidence of a sales arrangement, the product has been shipped or the services have been provided to the customer, the sales price is fixed or determinable, and collectibility is reasonably assured. We reduce our revenues for estimated customer returns and allowances, certain rebates, sales incentives and promotions in the same period the related sales are recorded.

We also record revenues generated under long-term, construction contracts, mainly in connection with the installation of specialized roofing and flooring systems, and related services. In general, we account for long-term, construction contracts under the percentage-of-completion method, and therefore record contract revenues and related costs as our contracts progress. This method recognizes the economic results of contract performance on a timelier basis than does the completed-contract method; however, application of this method requires reasonably dependable estimates of progress toward completion, as well as other dependable estimates. When reasonably dependable estimates cannot be made, or if other factors make estimates doubtful, the completed-contract method is applied. Under the completed-contract method, billings and costs are accumulated on the balance sheet as the contract progresses, but no revenue is recognized until the contract is complete or substantially complete.

***Translation of Foreign Currency Financial Statements and Foreign Currency Transactions***

Our reporting currency is the U.S. dollar. However, the functional currency for each of our foreign subsidiaries is its local currency. We translate the amounts included in our Consolidated Statements of Income from our foreign subsidiaries into U.S. dollars at weighted-average exchange rates, which we believe are representative of the actual exchange rates on the dates of the transactions. Our foreign subsidiaries' assets and liabilities are translated into U.S. dollars from local currency at the actual exchange rates as of the end of each reporting date, and we record the resulting foreign exchange translation adjustments in our Consolidated Balance Sheets as a component of accumulated other comprehensive income (loss). If the U.S. dollar continues to strengthen, we will continue to reflect the resulting losses as a component of accumulated other comprehensive income. Conversely, if the U.S. dollar were to weaken, foreign exchange translation gains could result, which would favorably impact accumulated other comprehensive income. Translation adjustments will be included in net earnings in the event of a sale or liquidation of any of our

underlying foreign investments, or in the event that we distribute the accumulated earnings of consolidated foreign subsidiaries. If we determined that the functional currency of any of our foreign subsidiaries should be the U.S. dollar, our financial statements would be affected. Should this occur, we would adjust our reporting to appropriately account for any such changes.

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As appropriate, we use permanently invested intercompany loans as a source of capital to reduce exposure to foreign currency fluctuations at our foreign subsidiaries. These loans, on a consolidated basis, are treated as being analogous to equity for accounting purposes. Therefore, foreign exchange gains or losses on these intercompany loans are recorded in accumulated other comprehensive income (loss). If we were to determine that the functional currency of any of our subsidiaries should be the U.S. dollar, we would no longer record foreign exchange gains or losses on such intercompany loans.

### ***Goodwill***

We apply the provisions of SFAS No. 141, *Business Combinations*, which addresses the initial recognition and measurement of goodwill and intangible assets acquired in a business combination. We also apply the provisions of SFAS No. 142, *Goodwill and Other Intangible Assets*, which requires that goodwill be tested at least on an annual basis, or more frequently as impairment indicators arise, using a fair-value approach at the reporting unit level. Our reporting units have been identified at the component level, or one level below our operating segments. We have elected to perform our annual required impairment tests, which involve the use of estimates related to the fair market values of the reporting units with which goodwill is associated, during our fourth fiscal quarter. Calculating the fair market values of reporting units requires our significant use of estimates and assumptions. We estimate the fair values of our reporting units by applying a combination of third-party market value indicators and discounted future cash flows to the respective reporting unit's annual projected earnings before interest, taxes, depreciation and amortization. In applying this methodology, we rely on a number of factors, including future business plans, actual and forecasted operating results, and market data. In the event that our calculations indicate that goodwill is impaired, a fair value estimate of each tangible and intangible asset would be established. This process would require the estimation of the discounted cash flows expected to be generated by each asset in addition to independent asset appraisals, as appropriate, and, if impaired, these balances would be written down to fair value. Our cash flow estimates are based on our historical experience and our internal business plans, and appropriate discount rates are applied. Losses, if any, resulting from goodwill impairment tests would be reflected in pre-tax income in our income statement. We have not incurred any such impairment losses to date.

### ***Other Long-Lived Assets***

We assess identifiable, non-goodwill intangibles and other long-lived assets for impairment whenever events or changes in facts and circumstances indicate the possibility that the carrying values of these assets may not be recoverable over their estimated remaining useful lives. Factors considered important in our assessment, which might trigger an impairment evaluation, include the following:

- significant under-performance relative to historical or projected future operating results;
- significant changes in the manner of our use of the acquired assets;
- significant changes in the strategy for our overall business; and
- significant negative industry or economic trends.

Additionally, we test all indefinite-lived intangible assets for impairment at least annually during our fiscal fourth quarter. Measuring a potential impairment of non-goodwill intangibles and other long-lived assets requires the use of various estimates and assumptions, including the determination of which cash flows are directly related to the assets being evaluated, the respective useful lives over which those cash flows will occur and potential residual values, if any. If we determine that the carrying values of these assets may not be recoverable based upon the existence of one or more of the above-described indicators or other factors, any impairment amounts would be measured based on the

projected net cash flows expected from these assets, including any net cash flows related to eventual disposition activities. The determination of any impairment losses would be based on the best information available, including internal estimates of discounted cash flows, quoted market prices, when available, and independent appraisals, as appropriate, to determine fair values. Cash flow estimates would be based on our historical experience and our internal business plans, with appropriate discount rates applied. We have not incurred any such impairment losses to date.

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***Deferred Income Taxes***

Our provision for income taxes is calculated in accordance with SFAS No. 109, Accounting for Income Taxes, which requires the recognition of deferred income taxes using the liability method. Deferred income taxes reflect the net tax effect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes and certain changes in valuation allowances. We provide valuation allowances against deferred tax assets if, based on available evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

In determining the adequacy of valuation allowances, we consider cumulative and anticipated amounts of domestic and international earnings or losses, anticipated amounts of foreign source income, as well as the anticipated taxable income resulting from the reversal of future taxable temporary differences.

We intend to maintain any recorded valuation allowances until sufficient positive evidence (for example, cumulative positive foreign earnings or additional foreign source income) exists to support a reversal of the tax valuation allowances.

***Contingencies***

We are party to claims and lawsuits arising in the normal course of business, including the various asbestos-related suits discussed in Note F to our Consolidated Financial Statements. Although we cannot precisely predict the amount of any liability that may ultimately arise with respect to any of these matters, we record provisions when we consider the liability probable and reasonably estimable. Our provisions are based on historical experience and legal advice, are reviewed quarterly and are adjusted according to developments. Estimating probable losses requires the analysis of multiple forecasted factors that often depend on judgments about potential actions by third parties, such as regulators, courts, and state and federal legislatures. Changes in the amounts of our loss provisions, which can be material, affect our Consolidated Statements of Income. Due to the inherent uncertainties in the process undertaken to estimate potential losses, we are unable to estimate an additional range of loss in excess of our accruals. While it is reasonably possible that such excess liabilities, if they were to occur, could be material to operating results in any given quarter or year of their recognition, we do not believe that it is reasonably possible that such excess liabilities would have a material adverse effect on our long-term results of operations, liquidity or consolidated financial position.

Our environmental-related accruals are similarly established and/or adjusted as more information becomes available upon which costs can be reasonably estimated. Here again, actual costs may vary from these estimates because of the inherent uncertainties involved, including the identification of new sites and the development of new information about contamination. Certain sites are still being investigated and, therefore, we have been unable to fully evaluate the ultimate costs for those sites. As a result, accruals have not been estimated for certain of these sites and costs may ultimately exceed existing estimated accruals for other sites. We have received indemnities for potential environmental issues from purchasers of certain of our properties and businesses and from sellers of some of the properties or businesses we have acquired. We have also purchased insurance to cover potential environmental liabilities at certain sites. If the indemnifying or insuring party fails to, or becomes unable to, fulfill its obligations under those agreements or policies, we may incur environmental costs in addition to any amounts accrued, which may have a material adverse effect on our financial condition, results of operations or cash flows.

Additionally, our operations are subject to various federal, state, local and foreign tax laws and regulations which govern, among other things, taxes on worldwide income. The calculation of our income tax expense is based on the best information available and involves our significant judgment. The actual income tax liability for each jurisdiction in any year can be, in some instances, determined ultimately several years after the financial statements have been published.

We maintain accruals for estimated income tax exposures for many different jurisdictions. Tax exposures are settled primarily through the resolution of audits within each tax jurisdiction or the closing of a statute of limitation. Tax exposures can also be affected by changes in applicable tax laws or other factors, which may cause us to believe a revision of past estimates is appropriate. We believe that appropriate liabilities have been established for income tax exposures; however, actual results may differ materially from our estimates.

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### ***Allowance for Doubtful Accounts Receivable***

An allowance for anticipated uncollectible trade receivable amounts is established using a combination of specifically identified accounts to be reserved and a reserve covering trends in collectibility. These estimates are based on an analysis of trends in collectibility, past experience and individual account balances identified as doubtful based on specific facts and conditions. Receivable losses are charged against the allowance when we confirm uncollectibility. Actual collections of trade receivables could differ from our estimates due to changes in future economic or industry conditions or specific customer's financial conditions.

### ***Inventories***

Inventories are stated at the lower of cost or market, cost being determined on a first-in, first-out (FIFO) basis and market being determined on the basis of replacement cost or net realizable value. Inventory costs include raw materials, labor and manufacturing overhead. We review the net realizable value of our inventory in detail on an on-going basis, with consideration given to various factors, which include our estimated reserves for excess, obsolete, slow moving or distressed inventories. If actual market conditions differ from our projections, and our estimates prove to be inaccurate, write-downs of inventory values and adjustments to cost of sales may be required. Historically, our inventory reserves have approximated actual experience.

### ***Marketable Securities***

Marketable securities, included in other current and long-term assets, are composed of available for sale securities and are reported at fair value, based on quoted market prices. Realized gains and losses on sales of investments are recognized in net income on the specific identification basis. Changes fair values of securities that are considered temporary, are recorded as unrealized gains and losses, net of applicable taxes, in accumulated other comprehensive income (loss) within stockholders' equity. Other-than-temporary declines in market value from original cost are reflected in operating income in the period in which the unrealized losses are deemed other than temporary. In order to determine whether an other-than-temporary decline in market value has occurred, the duration of the decline in value and our ability to hold the investment to recovery are considered in conjunction with an evaluation of the strength of the underlying collateral and the extent to which the investment's amortized cost or cost, as appropriate, exceeds its related market value.

## **REPORTABLE SEGMENT INFORMATION**

Our business is divided into two reportable segments: the industrial reportable segment and the consumer reportable segment. Within each reportable segment, we aggregate three operating segments that consist of individual groups of companies and product lines, which generally address common markets, share similar economic characteristics, utilize similar technologies and can share manufacturing or distribution capabilities. Our six operating segments represent components of our business for which separate financial information is available that is utilized on a regular basis by our chief executive officer in determining how to allocate the assets of the Company and evaluate performance. These six operating segments are each managed by an operating segment manager, who is responsible for the day-to-day operating decisions and performance evaluation of the operating segment's underlying businesses. We evaluate the profit performance of our segments primarily based on gross profit, and, to a lesser extent, income (loss) before income taxes, but also look to earnings (loss) before interest and taxes (EBIT) as a performance evaluation measure because interest expense is essentially related to corporate acquisitions, as opposed to segment operations.

Our industrial reportable segment products are sold throughout North America and also account for the majority of our international sales. Our industrial product lines are sold directly to contractors, distributors and end-users, such as industrial manufacturing facilities, public institutions and other commercial customers. This reportable segment

comprises three separate operating segments – our Tremco Group, StonCor Group, and RPM II/Industrial Group. Products and services within this reportable segment include construction chemicals, roofing systems, weatherproofing and other sealants, flooring and specialty chemicals.

Our consumer reportable segment manufactures and markets professional use and do-it-yourself ( DIY ) products for a variety of mainly consumer applications, including home improvement and personal leisure

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activities. Our consumer segment's major manufacturing and distribution operations are located primarily in North America. Consumer segment products are sold throughout North America directly to mass merchants, home improvement centers, hardware stores, paint stores, craft shops and to other smaller customers through distributors. This reportable segment comprises three operating segments — our DAP Group, Rust-Oleum/Zinsser Group, and RPM II/Consumer Group. Products within this reportable segment include specialty, hobby and professional paints; caulks; adhesives; silicone sealants; wood stains and specialty confectionary coatings and films.

In addition to our two reportable segments, there is a category of certain business activities and expenses, referred to as corporate/other, that does not constitute an operating segment. This category includes our corporate headquarters and related administrative expenses, results of our captive insurance companies, gains or losses on the sales of certain assets and other expenses not directly associated with either reportable segment. Assets related to the corporate/other category consist primarily of investments, prepaid expenses, deferred pension assets, and headquarters' property and equipment. These corporate and other assets and expenses reconcile reportable segment data to total consolidated income before income taxes, interest expense and earnings before interest and taxes.

The following table reflects the results of our reportable segments consistent with our management philosophy, and represents the information we utilize, in conjunction with various strategic, operational and other financial performance criteria, in evaluating the performance of our portfolio of product lines.

|   | <b>Quarter Ended<br/>November 30,</b> |                   | <b>Six Months Ended<br/>November 30,</b> |                     |
|---|---------------------------------------|-------------------|--|---------------------|
|   | <b>2008</b>                           | <b>2007</b>       | <b>2008</b>                              | <b>2007</b>         |
|   | <b>(In thousands)</b>                 |                   |  |                     |
| <b>Net Sales</b>                            |                                       |                   |  |                     |
| Industrial Segment                          | \$ 625,578                            | \$ 605,846        | \$ 1,323,160                             | \$ 1,214,446        |
| Consumer Segment                            | 264,387                               | 299,862           | 552,270                                  | 621,601             |
| <b>Consolidated</b>                         | <b>\$ 889,965</b>                     | <b>\$ 905,708</b> | <b>\$ 1,875,430</b>                      | <b>\$ 1,836,047</b> |
| <b>Gross Profit</b>                         |                                       |                   |  |                     |
| Industrial Segment                          | \$ 264,409                            | \$ 254,315        | \$ 556,184                               | \$ 509,859          |
| Consumer Segment                            | 92,317                                | 113,423           | 204,131                                  | 241,781             |
| <b>Consolidated</b>                         | <b>\$ 356,726</b>                     | <b>\$ 367,738</b> | <b>\$ 760,315</b>                        | <b>\$ 751,640</b>   |
| <b>Income (Loss) Before Income Taxes(a)</b> |                                       |                   |  |                     |
| Industrial Segment                          |                                       |                   |  |                     |
| Income Before Income Taxes(a)               | \$ 70,958                             | \$ 73,058         | \$ 162,470                               | \$ 152,710          |
| Interest (Expense), Net                     | (37)                                  | (915)             | (96)                                     | (1,657)             |
| EBIT(b)                                     | \$ 70,995                             | \$ 73,973         | \$ 162,566                               | \$ 154,367          |
| Consumer Segment                            |                                       |                   |  |                     |
| Income Before Income Taxes(a)               | \$ 14,806                             | \$ 29,819         | \$ 48,071                                | \$ 72,670           |
| Interest (Expense), Net                     | (1,074)                               | (994)             | (2,416)                                  | (1,850)             |
| EBIT(b)                                     | \$ 15,880                             | \$ 30,813         | \$ 50,487                                | \$ 74,520           |

|                                      |             |             |             |             |
|--------------------------------------|-------------|-------------|-------------|-------------|
| Corporate/Other                      |             |             |             |             |
| (Expense) Before Income Taxes(a)     | \$ (25,414) | \$ (21,964) | \$ (49,878) | \$ (44,318) |
| Interest (Expense), Net              | (16,283)    | (10,198)    | (25,468)    | (21,318)    |
| EBIT(b)                              | \$ (9,131)  | \$ (11,766) | \$ (24,410) | \$ (23,000) |
| <b>Consolidated</b>                  |             |             |             |             |
| Income (Loss) Before Income Taxes(a) | \$ 60,350   | \$ 80,913   | \$ 160,663  | \$ 181,062  |
| Interest (Expense), Net              | (17,394)    | (12,107)    | (27,980)    | (24,825)    |
| EBIT(b)                              | \$ 77,744   | \$ 93,020   | \$ 188,643  | \$ 205,887  |

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- (a) The presentation includes a reconciliation of Income (Loss) Before Income Taxes, a measure defined by generally accepted accounting principles ( GAAP ) in the U.S., to EBIT.
- (b) EBIT is defined as earnings before interest and taxes. We evaluate the profit performance of our segments based on income before income taxes, but also look to EBIT as a performance evaluation measure because interest expense is essentially related to corporate acquisitions, as opposed to segment operations. We believe EBIT is useful to investors for this purpose as well, using EBIT as a metric in their investment decisions. EBIT should not be considered an alternative to, or more meaningful than, operating income as determined in accordance with GAAP, since EBIT omits the impact of interest and taxes in determining operating performance, which represent items necessary to our continued operations, given our level of indebtedness and ongoing tax obligations. Nonetheless, EBIT is a key measure expected by and useful to our fixed income investors, rating agencies and the banking community all of whom believe, and we concur, that this measure is critical to the capital markets analysis of our segments' core operating performance. We also evaluate EBIT because it is clear that movements in EBIT impact our ability to attract financing. Our underwriters and bankers consistently require inclusion of this measure in offering memoranda in conjunction with any debt underwriting or bank financing. EBIT may not be indicative of our historical operating results, nor is it meant to be predictive of potential future results.

## **RESULTS OF OPERATIONS**

### ***Three Months Ended November 30, 2008***

#### ***Net Sales***

On a consolidated basis, net sales of \$890.0 million for the second quarter ended November 30, 2008 declined 1.7%, or \$15.7 million, over net sales of \$905.7 million during the same period last year. The organic decline in sales amounted to 4.6%, or \$41.7 million, of the shortfall in net sales over the prior year, which includes volume-related declines approximating 4.1% or \$37.3 million, and the impact of net unfavorable foreign exchange rates year-over-year, which amounted to 3.8%, or \$34.2 million, offset partially by pricing initiatives representing 3.3% of the prior year sales, or \$29.8 million. Foreign exchange losses resulted from the strong dollar against nearly all major foreign currencies, with the majority of the losses resulting from the weaker euro and Canadian dollar. Eight small acquisitions, net of the lost revenue related to the divestiture of our Bondo subsidiary during last year's second fiscal quarter, provided 2.9% of sales growth over last year, or \$26.0 million.

Industrial segment net sales, which comprised 70.3% of the current quarter's consolidated net sales, totaled \$625.6 million, growing 3.3% from last year's \$605.8 million. This segment's net sales growth resulted primarily from seven small acquisitions, which contributed 6.2% of the growth over the prior year. These improvements were offset by an overall decline in organic sales, which accounted for a decline of 2.9% over prior year sales, and included 4.3% from net unfavorable foreign exchange differences and volume declines approximating 1.9%, offset partially by 3.3% from pricing. The pure unit organic sales decline in the industrial segment resulted primarily from declines in domestic polymer flooring, exterior insulated finishing systems and certain specialty colorant and coatings product lines. There was continued growth during the quarter from ongoing industrial and commercial maintenance and improvement activities in Latin America, South Africa and the Middle East, in addition to slower, but continued, growth in global roofing products and services. Many of our industrial segment product lines, including corrosion control coatings and fiberglass reinforced plastics, continue to grow organic sales. Despite the impact of the continuing weak economic environment on certain sectors of our domestic commercial construction markets, which we expect will continue throughout the remainder of our current fiscal year, we continue to secure new business through strong brand offerings, new product innovations and international expansion.

Consumer segment net sales, which comprised 29.7% of the current quarter's consolidated net sales, decreased by 11.8% to \$264.4 million from \$299.9 million during last year's second quarter. Contributing to this segment's net sales decline was the impact of the divestiture of our Bondo subsidiary during last year's second fiscal quarter, which was only partially offset by recent acquisitions, for a net negative impact of 3.8%. Additionally, our consumer segment organic sales declined by 8.0%, which includes the impact of net unfavorable foreign exchange rates for approximately 2.7%, offset partially by pricing, which provided 3.3%. The organic sales volume decline reflects the

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continued weakness in the economy, including sluggish sales for retailers, as well as distributors impacted by the domestic housing recession. Our consumer segment continues to increase market penetration at major retail accounts with various new product launches, some of which occurred early in this year's first quarter, while also refocusing efforts on our various repair and maintenance products.

### *Gross Profit Margin*

Our consolidated gross profit declined to 40.1% of net sales this quarter from 40.6% of net sales for the same period a year ago, reflecting our overall net decline in sales volume, in addition to the impact of increased raw material costs, which were only partially offset by our recent price increases. Raw material costs reflect the impact of year-over-year increases in oil prices and energy costs, which have continued to put upward pressure on many of our raw material, packaging and transportation costs. Many of our key raw materials costs were higher than they were during the same period a year ago, such as plasticizers, epoxies, various solvents and resins. The impact of these higher raw material costs, net of price increases, weighed on our gross profit margin by approximately 1.4% percent of net sales, or 140 basis points ( bps ), but were offset partially by a slightly more favorable product mix and tighter spending controls. We began to experience some relief in certain raw material and transportation costs toward the end of this year's second quarter, as a result of declines in certain energy prices, which we anticipate will begin to impact our margins toward the end of our upcoming third fiscal quarter.

Our industrial segment gross profit for the second quarter of fiscal 2009 improved by 30 bps, to 42.3% of net sales from last year's second quarter result of 42.0% of net sales. Productivity gains, a favorable sales mix and tighter spending controls favorably impacted this segment's gross margin the current period. However, higher selling prices were more than offset by certain continued higher raw material costs during the quarter, for a net unfavorable impact of 70 bps.

Our consumer segment gross profit for the quarter declined to 34.9% of net sales from 37.8% of net sales last year, or approximately 290 bps, mainly as a result of the approximate 300 bps impact of higher raw material costs, net of recent price increases, combined with the unfavorable margin impact of this segment's organic sales volume decline versus last year's second quarter net sales. Partially offsetting the impact of these items was a favorable mix of sales compared with the prior year period.

### *Selling, General and Administrative Expenses ( SG&A )*

Our consolidated SG&A increased to 31.4% of net sales for the current quarter compared with 30.3% a year ago. The 110 bps increase in this margin primarily reflects the unfavorable margin impact from the overall unit volume decline in net sales, combined with additional bad debt, warranty and distribution expense over the prior year, offset partially by favorable environmental reserve adjustments and compensation-related reductions, including reductions relating to stock-based compensation. During the quarter, certain strategic initiatives were undertaken by certain of our businesses relating to headcount reductions, which resulted in severance-related costs approximating 20 bps for the quarter. Further reductions in workforce are expected to result in additional severance-related costs during our upcoming fiscal third quarter. We anticipate that these strategic reductions will favorably impact our margins beginning with the second half of the current fiscal year.

Our industrial segment SG&A increased to 31.0% of net sales for the current quarter from 29.8% last year, reflecting the impact of higher employment-related costs, including increased compensation and benefit-related accruals, and additional bad debt expense. Partially offsetting those items was certain favorable foreign exchange transactions. As discussed above, certain severance-related expenses were incurred during the current quarter, which approximated 10 bps for this segment.

Our consumer segment SG&A as a percentage of net sales for the current quarter increased by 130 bps to 28.8% compared with 27.5% a year ago, reflecting the unfavorable margin impact of the unit volume decline in net sales in this segment, in addition to certain strategic reductions in this segment's workforce which approximated 40 bps.

SG&A expenses in our corporate/other category decreased during the current quarter to \$9.2 million from \$11.8 million during the corresponding period last year. This decrease essentially reflects the impact of lower compensation-related expenses, including stock-based compensation, versus last year's second fiscal quarter.

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Partially offsetting these expense reductions was the combination of net unfavorable foreign currency adjustments and certain higher benefit-related expense.

License fee and joint venture income of approximately \$0.7 million and \$0.5 million for each of the quarters ended November 30, 2008 and 2007, respectively, are reflected as reductions of consolidated SG&A expenses.

We recorded total net periodic pension and postretirement benefit costs of \$5.8 million and \$4.9 million for the quarters ended November 30, 2008 and 2007, respectively. This increased pension expense of \$0.9 million was primarily the result of increased pension service and higher interest costs approximating \$0.7 million, along with net actuarial losses incurred of approximately \$0.2 million. We expect that pension expense will fluctuate on a year-to-year basis, depending primarily upon the investment performance of plan assets and potential changes in interest rates, but such changes are not expected to be material to our consolidated financial results.

### *Net Interest Expense*

Net interest expense was approximately \$5.3 million higher in the second quarter of fiscal 2009 than in the corresponding period of fiscal 2008, mainly as a result of a \$5.5 million unfavorable change from the prior year second quarter investment income of \$3.3 million versus the current quarter loss on investments of \$2.2 million. This unfavorable change includes the impact of net realized gains and losses on the sales of investments, which resulted in a net loss of \$1.6 million for the quarter ended November 30, 2008 and a net gain of \$1.2 million for the same period last year, as well as impairments recognized on securities that management has determined are other-than-temporary declines in value, which approximated \$2.6 million and \$57,000 for the quarters ended November 30, 2008 and 2007, respectively. The year over year changes in these items reflect the current global economic downturn and related declines in the U.S. financial markets. Additionally, interest rates averaged 6.0% overall during the quarter, compared with 5.4% in the prior year second quarter, which increased interest expense by approximately \$1.1 million, while our lower average borrowings this quarter reduced interest expense by approximately \$3.5 million versus last year's second quarter. We also had higher weighted-average net borrowings associated with recent acquisitions, approximating \$119.1 million during the quarter, which increased interest expense by approximately \$1.6 million, and other additional interest-related costs approximating \$0.6 million.

### *Income Before Income Taxes ( IBT )*

Our consolidated IBT for this year's second quarter declined to \$60.3 million versus last year's second quarter result of \$80.9 million, for a margin on net sales of 6.8% versus 9.0% a year ago.

Our industrial segment IBT decreased by 2.9%, to \$71.0 million from last year's \$73.1 million, reflecting this segment's 2.9% decline in organic sales during the quarter, as previously discussed, in addition to certain higher raw material costs, compensation and bad debt expense occurring during this year's second quarter. Our consumer segment IBT declined by 50.3%, to \$14.8 million from \$29.8 million last year, as a result of certain higher raw material costs and unfavorable foreign exchange adjustments.

### *Income Tax Rate*

Our effective income tax rate was 30.9% for the three months ended November 30, 2008 compared to an effective income tax rate of 32.2% for the three months ended November 30, 2007.

For the three months ended November 30, 2008 and, to a lesser extent for the three months ended November 30, 2007, the effective tax rate differed from the federal statutory rate principally due to decreases in taxes as a result of the impact of certain foreign operations on our U.S. taxes and the effect of lower tax rates in certain of our foreign

jurisdictions. The decreases in the effective tax rates were partially offset by provisions for valuation allowances associated with losses incurred by certain of our foreign businesses, state and local income taxes and other non-deductible business operating expenses.

As of November 30, 2008, we have determined, based on the available evidence, that it is uncertain whether we will be able to recognize certain deferred tax assets. Therefore, in accordance with the provisions of SFAS No. 109,

Accounting for Income Taxes, we intend to maintain the tax valuation allowance recorded at November 30, 2008 for certain deferred tax assets until sufficient positive evidence (for example, cumulative positive foreign earnings

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or additional foreign source income) exists to support the reversal of the tax valuation allowances. This valuation allowance relates to U.S. federal foreign tax credit carryforwards, certain foreign net operating losses and net foreign deferred tax assets recorded in purchase accounting. Any reversal of the valuation allowance that was recorded in purchase accounting would reduce goodwill.

### *Net Income*

Net income of \$41.7 million for the three months ended November 30, 2008 compares to \$54.9 million for the same period last year, for a net margin on sales of 4.7% for the current quarter compared to the prior year's 6.1% net margin on sales. The decline in net margin year-over-year resulted from the combined impact of declining sales volumes in both segments, higher raw material costs and unfavorable foreign exchange adjustments, offset partially by the impact of favorable acquisitions.

Diluted earnings per common share for this year's second quarter declined by 23.3% to \$0.33 from \$0.43 a year ago.

### ***Six Months Ended November 30, 2008***

#### *Net Sales*

On a consolidated basis, net sales of \$1.88 billion for the six months ended November 30, 2008 increased 2.2%, or \$39.5 million, over net sales of \$1.84 billion during the same period last year. Organic sales declined by 1.1%, or \$21.4 million, from last year, including volume-related declines approximating 3.3% or \$62.1 million, and the impact of net unfavorable foreign exchange rates year-over-year, which amounted to 0.7%, or \$13.0 million, offset partially by pricing initiatives representing 2.9%, or \$53.7 million. Foreign exchange losses resulted from the stronger dollar against nearly all major foreign currencies, with the majority of the losses resulting from the weaker Canadian dollar. Nine small acquisitions, net of the lost revenue related to the divestiture of our Bondo subsidiary during last year's second fiscal quarter, provided 3.3% of the sales growth over last year, or \$60.9 million.

Industrial segment net sales, which comprised 70.6% of consolidated net sales for this year's first half, totaled \$1.32 billion, an increase of 9.0% from last year's \$1.21 billion. This segment's net sales growth resulted primarily from seven small acquisitions, which contributed 7.5% of the growth over the prior year. Organic sales contributed 1.5% of the growth over prior year sales, including 3.0% from favorable pricing, offset partially by the combination of 0.7% from net unfavorable foreign exchange differences and volume declines approximating 0.8%.

Consumer segment net sales, which comprised 29.4% of the current year's consolidated net sales, decreased by 11.2% to \$552.3 million from \$621.6 million during last year's first six months. Contributing to this segment's net sales decline was the impact of the divestiture of our Bondo subsidiary during last year's second fiscal quarter, which was only partially offset by recent acquisitions, for a net negative impact of 4.8%. Additionally, our consumer segment organic sales declined by 6.4%, which includes the combined impact of net unfavorable foreign exchange rates for approximately 0.8% and a decline in sales volume amounting to approximately 8.3%, offset partially by pricing, which provided approximately 2.7%.

#### *Gross Profit Margin*

Our consolidated gross profit declined to 40.5% of net sales this first half from 40.9% of net sales for the same period a year ago, reflecting the impact of increased raw material costs, which were only partially offset by our recent price increases, for a net impact of approximately 100 bps. Partially offsetting those items was a more favorable mix of product sales during this year's first half versus the same period a year ago.

Our industrial segment gross profit for the first six months of fiscal 2009 was essentially flat at 42.0% of net sales for both six month periods. Higher selling prices net of certain continued higher raw material costs during the current year resulted in a net unfavorable impact on this segment's gross profit margin of approximately 50 bps. Productivity savings, a favorable sales mix and tighter spending controls favorably impacted this segment's gross margin the current period.

Our consumer segment gross profit for the first six months of fiscal 2009 declined to 36.9% of net sales from 38.9% of net sales last year, or approximately 200 bps, mainly as a result of the approximate 230 bps impact of

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higher raw material costs, net of recent price increases, combined with this segment's organic sales volume decline over last year's first six months' net sales. Partially offsetting the impact of these items was a favorable mix of sales compared with the prior year period.

### *SG&A*

Our consolidated SG&A increased to 30.4% of net sales for the first six months of fiscal 2009 compared with 29.7% a year ago. The 70 bps increase in this margin primarily reflects the impact of the overall unit volume decline in net sales, combined with additional warranty-related expense and prior year favorable adjustments to certain insurance-related loss reserves, which did not recur this year. These additional expenses were partially offset by reductions in advertising and legal expense, in addition to favorable reductions in certain environmental-related accruals. As discussed in relation to the second quarter results, certain strategic initiatives were undertaken by some of our businesses relating to headcount reductions, which resulted in severance-related costs approximating 30 bps for the current six month period. Further reductions in workforce are expected to result in additional severance-related costs during our upcoming fiscal third quarter. We anticipate that these strategic reductions will favorably impact our margins beginning with the second half of the current fiscal year.

Our industrial segment SG&A increased to 29.7% of net sales for the first half of the current fiscal year from 29.3% last year, reflecting the impact of higher employment-related costs, including increased compensation and benefit-related accruals, higher warranty-related expense, and additional bad debt expense over the prior year period. Partially offsetting those items was certain favorable foreign exchange transactions during the current year's first six months. As discussed above, certain severance-related expenses were incurred during the current six month period, which approximated 20 bps for this segment.

Our consumer segment SG&A as a percentage of net sales for the first half of the current fiscal year increased by 90 bps to 27.8% compared with 26.9% a year ago, reflecting the unit volume decline in net sales in this segment, in addition to certain strategic reductions in this segment's workforce which approximated 40 bps.

SG&A expenses in our corporate/other category increased during the first six months of fiscal 2009 to \$24.6 million from \$23.0 million during the corresponding period last year. This increase essentially reflects the impact of net unfavorable foreign currency adjustments, certain higher benefit-related expense and prior year favorable insurance-related loss reserve adjustments, which did not recur this year, partially offset by this year's lower legal expenses versus last year's first half.

License fee and joint venture income of approximately \$1.5 million and \$1.1 million for each of the six month periods ended November 30, 2008 and 2007, respectively, are reflected as reductions of consolidated SG&A expenses.

We recorded total net periodic pension and postretirement benefit costs of \$11.4 million and \$9.7 million for the six month periods ended November 30, 2008 and 2007, respectively. This increased pension expense of \$1.7 million was primarily the result of higher interest costs approximating \$1.3 million, along with net actuarial losses incurred of approximately \$0.4 million. We expect that pension expense will fluctuate on a year-to-year basis, depending primarily upon the investment performance of plan assets and potential changes in interest rates, but such changes are not expected to be material to our consolidated financial results.

### *Net Interest Expense*

Net interest expense was approximately \$3.2 million higher in the first half of fiscal 2009 than in the corresponding period of fiscal 2008, mainly as a result of a \$4.7 million unfavorable change from the prior year first six months investment income of \$6.6 million versus \$1.9 million during this year's first half. This unfavorable change includes

the impact of net realized gains and losses on the sales of investments, which resulted in a net gain of \$1.3 million for the six months ended November 30, 2008 and a net gain of \$2.1 million for the same period last year, as well as impairments recognized on securities that management has determined are other-than-temporary declines in value, which approximated \$3.4 million and \$0.1 million for the first half of fiscal 2009 and 2008, respectively. As previously discussed, the year over year changes in these items reflect the current global economic downturn and related declines in the U.S. financial markets. We also recognized approximately \$0.6 million less

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interest and dividend income during this year's first half versus the same period last year. Offsetting those losses was the impact of lower interest rates, which averaged 5.7% overall during the current period, compared with 6.0% in the prior year first half, causing interest expense to decrease by approximately \$1.8 million, while our lower average borrowings during the current period reduced interest expense by an additional \$4.0 million. Higher weighted-average net borrowings associated with recent acquisitions, approximating \$122.9 million during the current period, which increased interest expense by approximately \$3.2 million, and other additional interest-related costs approximating \$1.1 million.

***IBT***

Our consolidated IBT for this year's first half declined to \$160.6 million versus \$181.1 million during last year's first half, for a margin of 8.6% of net sales versus 9.9% a year ago.

Our industrial segment IBT increased by 6.4%, to \$162.5 million from last year's \$152.7 million, reflecting this segment's 1.5% growth in organic sales over the prior year period, as previously discussed, offset partially by certain higher raw material costs, warranty expense, compensation-related expense and bad debt occurring during this year's first half. Our consumer segment IBT declined by 33.9%, to \$48.1 million from \$72.7 million last year, primarily as a result of declining sales volumes combined with net higher raw material costs.

***Income Tax Rate***

The effective income tax rate was 30.8% for the six months ended November 30, 2008 compared to an effective income tax rate of 32.0% for the six months ended November 30, 2007.

For the six months ended November 30, 2008 and, to a lesser extent for the six months ended November 30, 2007, the effective tax rate differed from the federal statutory rate principally as a result of the impact of certain foreign operations on our U.S. taxes and the effect of lower tax rates in certain of our foreign jurisdictions. The decreases in the effective tax rates were partially offset by valuation allowances associated with losses incurred by certain of our foreign businesses, state and local income taxes and other non-deductible business operating expenses.

As described in this Management's Discussion and Analysis of Financial Condition and Results of Operations for the three month period ended November 30, 2008, there is uncertainty as to whether we will be able to recognize certain deferred tax assets. Refer to the section of this filing mentioned above for further information.

***Net Income***

Net income of \$111.2 million for the six months ended November 30, 2008 compares to \$123.1 million for the same period last year for a net margin on sales of 5.9% for the current period compared to the prior period's 6.7% net margin on sales. The decline in net margin year-over-year resulted from the combined impact of declining sales volumes in both segments, higher raw material costs and unfavorable foreign exchange adjustments, offset partially by the impact of favorable acquisitions.

Diluted earnings per common share for this year's first six months declined by 10.4% to \$0.86 from \$0.96 a year ago.

**LIQUIDITY AND CAPITAL RESOURCES**

***Cash Flows From:***

***Operating Activities***

Operating activities provided cash flow of \$104.0 million during the first six months of the current fiscal year compared with \$104.1 million of cash flow provided during the same period of fiscal 2008.

A lower trade accounts receivable balance at the end of the current six month period, resulting from additional cash collections, provided \$212.1 million in cash versus \$120.3 million last year, or approximately \$91.8 million more cash year over year. Inventory balances increased during both the current and prior year periods, which

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required \$15.6 million of cash this year versus \$29.1 million last year, or \$13.5 million less cash year-over-year. Finally, we used \$45.1 million more for accounts payable during this year's first six months compared to the same period a year ago, as a result of a change in the timing of certain payments and increased activity levels.

Cash provided from operations, along with the use of available credit lines, as required, remain our primary sources of liquidity.

## **Investing Activities**

Capital expenditures, other than for ordinary repairs and replacements, are made to accommodate our continued growth to achieve production and distribution efficiencies, to expand capacity and to enhance our administration capabilities. Capital expenditures of \$24.9 million during this year's first six months compare with current-year depreciation of \$32.2 million. Capital spending is expected to decline to a level which will trail depreciation expense at least through fiscal 2010. Due to additional capacity, which has been brought on-line over the last several years, we believe there is adequate production capacity to meet our needs based on anticipated growth rates. Any additional capital expenditures made over the next few years will likely relate primarily to new products and technology.

Our captive insurance companies invest their excess cash in marketable securities in the ordinary course of conducting their operations, and this activity will continue. Differences in the amounts related to these activities on a year-over-year basis are primarily attributable to differences in the timing and performance of their investments balanced against amounts required to satisfy claims. At November 30, 2008, the fair value of our investments in marketable securities totaled \$69.8 million, of which investments with a fair value of \$44.7 million were in an unrealized loss position. At May 31, 2008, the fair value of our investments in marketable securities totaled \$110.4 million, of which investments with a fair value of \$25.8 million were in an unrealized loss position. Total unrealized losses recorded in accumulated other comprehensive income at November 30, 2008 and May 31, 2008 were \$23.6 million and \$1.7 million, respectively. We regularly review our marketable securities in unrealized loss positions in order to determine whether or not we have the ability and intent to hold these investments until their cost can be recovered. That determination is based upon the severity and duration of the decline, in addition to our evaluation of the cash flow requirements of our businesses. Unrealized losses at November 30, 2008 were generally caused by the recent decline in valuations in the financial sector and the volatility in the global economy, specifically over the last few months of our recently completed second fiscal quarter. If general economic conditions were to continue to deteriorate, including continued uncertainties surrounding the volatility in financial markets and the viability of banks and other financial institutions, and if we were to experience continuing or significant additional unrealized losses within our portfolio of investments in marketable securities, we may recognize additional other-than-temporary impairment losses in future periods. Such potential losses could have a material impact on our results of operations. As such, we continue to closely evaluate the status of our investments and our ability and intent to hold these investments until their cost can be recovered.

## **Financing Activities**

On February 20, 2008 we issued and sold \$250.0 million of 6.50% Notes due February 15, 2018. The proceeds were used to repay our \$100.0 million Senior Unsecured Notes due March 1, 2008, the outstanding principal under our \$125.0 million accounts receivable securitization program and \$19.0 million in short-term borrowings under our revolving credit facility. This financing strengthened our credit profile and liquidity position, as well as lengthened the average maturity of our outstanding debt obligations.

On December 29, 2006, we replaced our \$330.0 million revolving credit facility with a \$400.0 million five-year credit facility (the "Credit Facility"). The Credit Facility is used for working capital needs and general corporate purposes, including acquisitions. The Credit Facility provides for borrowings in U.S. dollars and several foreign currencies and

provides sublimits for the issuance of letters of credit in an aggregate amount of up to \$35.0 million and a swing-line of up to \$20.0 million for short-term borrowings of less than 15 days. In addition, the size of the Credit Facility may be expanded, subject to lender approval, upon our request by up to an additional \$175.0 million, thus potentially expanding the Credit Facility to \$575.0 million.

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We are exposed to market risk associated with interest rates. We do not use financial derivative instruments for trading purposes, nor do we engage in foreign currency, commodity or interest rate speculation. Concurrent with the issuance of our 6.7% Senior Unsecured Notes, RPM United Kingdom G.P. entered into a cross currency swap, which fixed the interest and principal payments in euros for the life of the 6.7% Senior Unsecured Notes and resulted in an effective euro fixed rate borrowing of 5.31%. In addition to hedging the risk associated with our 6.7% Senior Unsecured Notes, our only other hedged risks are associated with certain fixed debt, whereby we have a \$200.0 million notional amount interest rate swap contract designated as a fair value hedge to pay floating rates of interest, based on six-month LIBOR that matures in our fiscal year ending May 31, 2010. Because critical terms of the debt and interest rate swap match, the hedge is considered perfectly effective against changes in fair value of debt, and therefore, there is no need to periodically reassess the effectiveness during the term of the hedge.

Our available liquidity, including our cash and short-term investments and amounts available under our committed credit facilities, stood at \$523.4 million at November 30, 2008. Our debt-to-capital ratio was 46.2% at November 30, 2008, compared with 48.6% at May 31, 2008.

During the first quarter of fiscal 2009, we called for redemption all of our outstanding Senior Convertible Notes due May 13, 2033. Prior to the redemption, virtually all of the holders converted their Senior Convertible Notes into shares of our common stock. For additional information, refer to Note L, Convertible Notes, to the Consolidated Financial Statements.

The following table summarizes our financial obligations and their expected maturities at November 30, 2008 and the effect such obligations are expected to have on our liquidity and cash flow in the periods indicated.

**Contractual Obligations**

|  | <b>Total<br/>Contractual<br/>Payment<br/>Stream</b> | <b>2009</b>       | <b>Payments Due in</b> |                   | <b>After 2013</b> |
|--|---|-------------------|------------------------|-------------------|-------------------|
|  |   |                   | <b>2010-11</b>         | <b>2012-13</b>    |                   |
|  |   |                   | <b>(In thousands)</b>  |                   |                   |
| Long-term debt obligations                           | \$ 962,611  | \$ 171,247        | \$ 1,977               | \$ 189,604        | \$ 599,783        |
| Capital lease obligations                            | 4,631   | 764               | 1,361                  | 1,237             | 1,269             |
| Operating lease obligations                          | 134,442   | 34,165            | 43,967                 | 21,962            | 34,348            |
| Other long-term liabilities(1):                      |   |                   |                        |                   |                   |
| Interest payments on long-term debt obligations      | 274,826   | 42,328            | 74,374                 | 68,124            | 90,000            |
| Contributions to pension and postretirement plans(2) | 213,600   | 18,700            | 38,300                 | 52,700            | 103,900           |
| <b>Total</b>   | <b>\$ 1,590,110</b>                                 | <b>\$ 267,204</b> | <b>\$ 159,979</b>      | <b>\$ 333,627</b> | <b>\$ 829,300</b> |

- (1) Excluded from other long-term liabilities is our liability for unrecognized tax benefits, which totaled \$4.7 million at November 30, 2008. Currently, we cannot predict with reasonable reliability the timing of cash settlements to the respective taxing authorities.

- (2) These amounts represent our estimated cash contributions to be made in the periods indicated for our pension and postretirement plans, assuming no actuarial gains or losses, assumption changes or plan changes occur in any period. The projection results assume \$10.2 million will be contributed to the U.S. plans in fiscal 2009; all other plans and years assume the required minimum contribution will be contributed. Also included are expected interest payments on long-term debt.

We maintain excellent relations with our banks and other financial institutions to help provide continuous access to financing for future growth opportunities and other corporate purposes.

***Off-Balance Sheet Arrangements***

We do not have any off-balance sheet financings, other than the minimum operating lease commitments included per the above Contractual Obligations table. We have no subsidiaries that are not included in our financial

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statements, nor do we have any interests in or relationships with any special purpose entities that are not reflected in our financial statements.

**OTHER MATTERS**

***Environmental Matters***

Environmental obligations continue to be appropriately addressed and, based upon the latest available information, it is not anticipated that the outcome of such matters will materially affect our results of operations or financial condition. Our critical accounting policies and estimates set forth above describe our method of establishing and adjusting environmental-related accruals and should be read in conjunction with this disclosure. For additional information, refer to Part II, Item 1. Legal Proceedings.

**FORWARD-LOOKING STATEMENTS**

The foregoing discussion includes forward-looking statements relating to our business. These forward-looking statements, or other statements made by us, are made based on our expectations and beliefs concerning future events impacting us and are subject to uncertainties and factors (including those specified below), which are difficult to predict and, in many instances, are beyond our control. As a result, our actual results could differ materially from those expressed in or implied by any such forward-looking statements. These uncertainties and factors include (a) general economic conditions, including uncertainties surrounding the volatility in financial markets, the availability of capital and the effect of changes in interest rates, and the viability of banks and other financial institutions; (b) the price, supply and capacity of raw materials, including assorted pigments, resins, solvents, and other natural gas and oil based materials; packaging, including plastic containers; and transportation services, including fuel surcharges; (c) continued growth in demand for our products; (d) legal, environmental and litigation risks inherent in our construction and chemicals businesses and risks related to the adequacy of our insurance coverage for such matters; (e) the effect of fluctuations in currency exchange rates upon our foreign operations; (f) the effect of non-currency risks of investing in and conducting operations in foreign countries, including those relating to domestic and international political, social, economic and regulatory factors; (g) risks and uncertainties associated with our ongoing acquisition and divestiture activities; (h) risks related to the adequacy of our contingent liabilities, including for asbestos-related claims; and (i) other risks detailed in our filings with the Securities and Exchange Commission, including the risk factors set forth in our Annual Report on Form 10-K for the year ended May 31, 2008, as the same may be updated from time to time. We do not undertake any obligation to publicly update or revise any forward-looking statements to reflect future events, information or circumstances that arise after the filing date of this document.

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

We are exposed to market risk from changes in raw materials costs, interest rates and foreign exchange rates since we fund our operations through long- and short-term borrowings and conduct our business in a variety of foreign currencies. There were no material potential changes in our exposure to these market risks since May 31, 2008.

**ITEM 4. *CONTROLS AND PROCEDURES***

**(a) EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES.**

Our Chief Executive Officer and Chief Financial Officer, after evaluating the effectiveness of our disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e)) as of November 30, 2008 (the Evaluation Date), have concluded that as of the Evaluation Date, our disclosure controls and procedures were effective in ensuring that

information required to be disclosed by us in the reports we file or submit under the Exchange Act (1) is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms, and (2) is accumulated and communicated to our management, including the Chief Executive Officer and the Chief Financial Officer, as appropriate to allow for timely decisions regarding required disclosure.

(b) CHANGES IN INTERNAL CONTROL.

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There were no changes in our internal control over financial reporting that occurred during the fiscal quarter ended November 30, 2008 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**PART II OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS**

**Asbestos Litigation**

Certain of our wholly-owned subsidiaries, principally Bondex International, Inc. (collectively referred to as our subsidiaries), are defendants in various asbestos-related bodily injury lawsuits filed in various state courts with the vast majority of current claims pending in six states — Texas, Florida, Mississippi, Maryland, Illinois and Ohio. These cases generally seek unspecified damages for asbestos-related diseases based on alleged exposures to asbestos-containing products previously manufactured by our subsidiaries or others.

As of November 30, 2008, our subsidiaries had a total of 10,048 active asbestos cases compared to a total of 11,117 cases as of November 30, 2007. For the quarter ended November 30, 2008, our subsidiaries secured dismissals and/or settlements of 1,824 cases and made total payments of \$16.4 million, which included defense-related payments of \$6.1 million. For the comparable period ended November 30, 2007, dismissals and/or settlements covered 292 cases and total payments were \$26.1 million, which included defense-related payments of \$13.8 million. For the six months ended November 30, 2008, our subsidiaries secured dismissals and/or settlements of 2,025 cases and made total payments of \$32.4 million, which included defense-related payments of \$12.8 million. For the comparable period ended November 30, 2007, dismissals and/or settlements covered 657 cases and total payments were \$48.9 million, which included defense-related payments of \$22.6 million.

Of the 1,824 cases that were dismissed in the quarter ended November 30, 2008, 1,420 were non-malignancies or unknown disease cases that had been maintained on an inactive docket in Ohio and were administratively dismissed by the Cuyahoga County Court of Common Pleas. These claims were dismissed without prejudice and may be re-filed should the claimants involved be able to demonstrate disease in accordance with medical criteria laws established in the state of Ohio.

During the prior fiscal year, our subsidiaries incurred higher year-over-year, defense-related payments as a result of implementing various changes to our management and defense of asbestos claims, including a transition to a new claims intake and database service provider. To facilitate that transition and other related changes, we incurred duplicate defense-related payments approximating \$3.0 million during last year's second fiscal quarter. The transition was completed during the quarter ended February 29, 2008.

Excluding defense-related payments, the average payment made to settle or dismiss a case approximated \$6,000 and \$42,000 for each of the quarters ended November 30, 2008 and 2007, respectively. As discussed above, there were approximately 1,420 non-malignancies or unknown disease cases that were administratively dismissed during the current fiscal quarter. Excluding those dismissed cases, the average payment made to settle or dismiss a case approximated \$25,000 for the quarter ended November 30, 2008. The amount and timing of dismissals and settlements can fluctuate significantly from period to period, resulting in volatility in the average cost to resolve a case in any given quarter or year. In addition, in some jurisdictions, cases may involve more than one individual claimant. As a result, settlement or dismissal payments made on a per case basis are not necessarily reflective of the payment amounts on a per claimant basis. For example, the amount paid to settle or dismiss a case can vary widely depending on a variety of factors, including the mix of malignancy and non-malignancy claimants, and the amount of defense expenditures incurred during the period.

For additional information on our asbestos litigation, including a discussion of our asbestos related loss contingencies and a discussion of certain of our subsidiaries complaint against certain third-party insurers, see Note F of the Notes to Consolidated Financial Statements.

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### **EIFS Litigation**

As of November 30, 2008, Dryvit, one of our wholly owned subsidiaries, was a defendant or co-defendant in various single family residential exterior insulated finish systems ( EIFS ) cases, the majority of which are pending in the southeastern region of the country. Dryvit is also defending EIFS lawsuits involving commercial structures, townhouses and condominiums. The vast majority of Dryvit s EIFS lawsuits seek monetary relief for water intrusion related property damages, although some claims in certain lawsuits allege personal injuries from exposure to mold.

Third party excess insurers have historically paid varying shares of Dryvit s defense and settlement costs in the individual commercial and residential EIFS lawsuits under various cost-sharing agreements. Dryvit has assumed a greater share of the costs associated with its EIFS litigation as it seeks funding commitments from our third party excess insurers and will likely continue to do so pending the outcome of coverage litigation involving these same third party insurers. In accordance with a Court order, the parties filed dispositive motions on certain of the coverage issues. Oral argument on these motions was completed on September 2, 2008. The parties currently await a ruling on their respective summary judgment motions, after which they will participate in a court-ordered and agreed mediation. Discovery is stayed in the meantime. A trial date has not yet been scheduled. If mediation is not successful, the parties will resume discovery and a trial date will be scheduled.

### **Environmental Proceedings**

As previously reported, several of our subsidiaries are, from time to time, identified as a potentially responsible party under the federal Comprehensive Environmental Response, Compensation and Liability Act and similar state environmental statutes. In some cases, our subsidiaries are participating in the cost of certain clean-up efforts or other remedial actions. Our share of such costs, however, has not been material and we believe that these environmental proceedings will not have a material adverse effect on our consolidated financial condition or results of operations. See Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations Other Matters, in Part I of this Quarterly Report on Form 10-Q.

In October 2008, the Commonwealth of Massachusetts, acting through its Attorney General and Department of Environmental Protection, entered into a Settlement Agreement (the Settlement Agreement ) with Mantrose-Hauser Co., Inc. ( Mantrose ) and Zinsser Co., Inc. ( Zinsser ), concerning alleged violations by Mantrose and Zinsser (as successor to Mantrose) of certain environmental laws and regulations, including the Massachusetts Hazardous Waste Management Act, the Massachusetts Clean Waters Act, the Massachusetts Toxics Use Reduction Act, and the Massachusetts Oil and Hazardous Material Release Prevention and Response Act (collectively, the Massachusetts Environmental Laws ), at Zinsser s facility in Attleboro, Massachusetts (the Attleboro Facility ). In response, in part, to the alleged violations, Zinsser has elected to withdraw from manufacturing at the Attleboro Facility certain of its products. Further, pursuant to the Settlement Agreement, Zinsser has agreed to pay a cash penalty of \$2.0 million to the Commonwealth of Massachusetts, and has agreed to certain stipulated penalties in the event it violates the terms of the Settlement Agreement. Zinsser also agreed to take certain actions with respect to the Attleboro Facility, including complying with the Massachusetts Environmental Laws, developing and submitting updated air and water permit applications and making certain improvements at the Attleboro Facility relating to those applications, developing and implementing an environmental management system, and conducting an environmental compliance audit. Furthermore, Zinsser agreed to fund two supplemental environmental projects for the City of Attleboro, including providing \$150,000 to the Northeast States for Coordinated Air Use Management for the installation of auxiliary power units on certain diesel-powered locomotives to help reduce particulate emissions in and around the City of Attleboro, and providing \$150,000 for various waterfront improvements for the City of Attleboro. Zinsser has also separately agreed to donate certain parcels of the Attleboro Facility to the City of Attleboro, the terms of which donation are not set forth in the Settlement Agreement.

**ITEM 1A. *RISK FACTORS***

In addition to the other information set forth in this report, you should carefully consider the risk factors disclosed in Item 1A of our Annual Report on Form 10-K for the fiscal year ended May 31, 2008.

**Table of Contents****ITEM 2. UNREGISTERED SALE OF EQUITY SECURITIES AND USE OF PROCEEDS**

(c) The following table presents information about repurchases of common stock we made during the second quarter of fiscal 2009:

| Period                                       | Total Number<br>of Shares<br>Purchased(1) | Average<br>Price<br>Paid per<br>Share | Total Number<br>of Shares<br>Purchased as<br>Part of<br>Publicly<br>Announced<br>Plans or<br>Programs | Maximum<br>Number<br>of<br>Shares<br>that<br>May Yet<br>be<br>Purchased<br>Under the<br>Plans or<br>Programs(2) |
|--|---|---------------------------------------|---|---|
|  |   |                                       |   |   |
| September 1, 2008 through September 30, 2008 | 105,400                                   | \$ 20.35                              | 105,400   |   |
| October 1, 2008 through October 30, 2008     | 1,133,697                                 | \$ 16.27                              | 1,040,724   |   |
| November 1, 2008 through November 30, 2008   | 457                                       | \$ 14.28                              |   |   |
| Total-Second Quarter                         | 1,239,554                                 | \$ 16.62                              | 1,146,124   |   |

(1) A total of 93,430 shares of common stock reported as purchased are attributable to shares of common stock that were disposed of back to us in satisfaction of tax obligations related to the vesting of restricted stocks which were granted under RPM International Inc.'s 2004 Omnibus Equity Plan, the 2003 Restricted Stock Plan for Directors, the 1997 Restricted Stock Plan and the 2007 Restricted Stock Plan. The remaining 1,146,124 shares of common stock reported as purchased are attributable to our stock repurchase program.

(2) Refer to Note K of the Notes to Consolidated Financial Statements for further information regarding our stock repurchase program.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

The Company previously disclosed the results of the matters voted upon at its Annual Meeting of Stockholders held on October 10, 2008 (the "Annual Meeting") in a Current Report on Form 8-K filed on October 16, 2008. For the results of the voting at the Annual Meeting, please see the Company's October 16, 2008 Form 8-K.

**ITEM 6. EXHIBITS****Exhibit**

| Number | Description  |
|--------|--|
| 3.1    | Amended and Restated By-Laws of RPM International Inc., which are incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K, as filed with the Securities and Exchange Commission on October 17, 2008 (File No. 001-14187). |
| 10.1   | Form of Performance-Earned Restricted Stock (PERS) and Escrow Agreement.(x)  |
| 10.2   | Form of Stock Appreciation Rights Agreement.(x)  |
| 10.3   | Separation Agreement and General Release by and between the Company and Mr. Ernest Thomas, dated as of October 31, 2008.(x)  |
| 31.1   | Rule 13a-14(a) Certification of the Company's Chief Executive Officer.(x)  |
| 31.2   | Rule 13a-14(a) Certification of the Company's Chief Financial Officer.(x)  |
| 32.1   | Section 1350 Certification of the Company's Chief Executive Officer.(x)  |
| 32.2   | Section 1350 Certification of the Company's Chief Financial Officer.(x)  |

(x) Filed herewith.

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**RPM International Inc.**

Frank C. Sullivan  
President and Chief Executive Officer

By: /s/ Frank C. Sullivan

P. Kelly Tompkins  
Executive Vice President Administration and  
Chief Financial Officer

By: /s/ P. Kelly Tompkins

Dated: January 8, 2009