VALSPAR CORP
Form 10-K
December 20, 2013

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

# FORM 10-K

(Mark One)

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended October 25, 2013

**or**

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ______________________ to __________________

Commission File Number 1-3011

# THE VALSPAR CORPORATION

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **Delaware** | **36-2443580** |
| (State of incorporation) | (I.R.S. Employer Identification No.) |
| **901 3rd Avenue South** | |
| **Minneapolis, Minnesota** | **55402** |
| (Address of principal executive offices) | (Zip Code) |

Registrant s telephone number, including area code: (612) 851-7000

**Securities registered pursuant to Section 12(b) of the Act:**

| **Title of Each Class** | **Name of Each Exchange on which Registered** |
|---|---|
| Common Stock, $.50 Par Value | New York Stock Exchange |

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
x Yes o No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.
o Yes x No

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 the filing requirements for the past 90 days.
x Yes o No

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

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 definition of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x Accelerated filer o Non-accelerated filer o Smaller reporting company o
Indicate by check mark whether the registrant is a shell company (as defined in Rule12b-2 of the Act). oYes x No

The aggregate market value of the voting stock held by persons other than officers, directors and more than 10% stockholders of the registrant as of April 26, 2013 was approximately $3.9 billion based on the closing sales price of $63.58 per share as reported on the New York Stock Exchange. As of December 10, 2013, 85,401,609 shares of Common Stock, $0.50 par value per share (net of 33,041,015 shares in treasury), were outstanding.

**DOCUMENTS INCORPORATED IN PART BY REFERENCE**

Portions of The Valspar Corporation s definitive Proxy Statement (the Proxy Statement ), to be filed with the Securities and Exchange Commission within 120 days after the end of the fiscal year ended October 25, 2013, are incorporated by reference into Part III to the extent described in this report.

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# PART I

## ITEM 1 BUSINESS

### BUSINESS & PRODUCT OVERVIEW

The Valspar Corporation is a global leader in the paint and coatings industry. With fiscal 2013 net sales of $4,103.8 million, we believe we are the fifth largest paint and coatings supplier in the world. We manufacture and distribute a broad range of coatings, paints and related products, and we operate our business in two reportable segments: Coatings and Paints. Net sales for our Coatings and Paints segments in 2013 were $2,209.5 million and $1,671.2 million, respectively. We have grown our business internally and through acquisitions, focusing on the needs of our customers and investing in our brands and proprietary technology.

The Valspar Corporation is a Delaware corporation and was founded in 1806. Our principal executive offices are located at 901 3rd Avenue South, Minneapolis, Minnesota 55402, and our telephone number at that address is (612) 851-7000. Our corporate website address is www.valsparglobal.com. The information on our website is not part of this filing.

**Coatings Segment**

Our Coatings segment includes our industrial product lines and our packaging product line. We offer a broad range of decorative and protective coatings for metal, wood and plastic, primarily for sale to original equipment manufacturing (OEM) customers in Asia, Australia, Europe, North America and South America. Products within our Coatings segment include primers, top coats, varnishes, sprays, stains, fillers and other coatings used by customers in a wide range of manufacturing industries, including agricultural and construction equipment, appliances, building products, furniture, metal fabrication, metal packaging and transportation.

We utilize a wide variety of technologies to provide differentiated coatings that meet our customers requirements and enable value creation within the markets in which they are used. These technologies include electrodeposition, powder, solvent-based, waterborne, UV curing and laser sintering. Our capability to design and manufacture resins allows us to customize products and provide leading solutions for a range of market applications.

Our industrial product lines include coil, general industrial and wood. Our coil product line produces coatings that are applied to metal coils used to manufacture pre-engineered buildings and building components, other metal building and architectural products and appliances. Our general industrial product line provides customers a single source for powder, liquid and electrodeposition coatings technologies in a wide variety of industries, including agricultural and construction equipment, pipe, lawn and garden, appliance, transportation, and marine shipping containers. Our wood product line supplies decorative and protective coatings for wood furniture, building products, cabinets and floors. We also provide color design and technical service to our customers. We supply our industrial products throughout the world.

Our packaging product line includes coatings for the interior and exterior of packaging containers, principally metal food containers and beverage cans. We also produce coatings for aerosol and paint cans, crowns for glass bottles, plastic packaging and bottle closures. We believe we are the world s largest supplier of metal packaging coatings. We supply our packaging products throughout the world.

**Paints Segment**

Our Paints segment includes a wide variety of products such as paints, primers, topcoats and aerosol spray paints sold primarily through retailers, distribution networks and company-owned stores. This segment includes our consumer paints and automotive refinish product lines.

Our consumer paints product line comprises the largest part of our Paints segment. We offer a broad portfolio of interior and exterior decorative paints, stains, primers, varnishes, high performance floor paints and specialty decorative products, such as enamels, aerosols and faux finishes, used in both the do-it-yourself and professional markets. In the U.S. and Canada, we offer our branded products and private label brands for customers. The primary distribution channels for these products are home centers, hardware wholesalers, distributors and independent dealers. In China, we sell Huarun branded consumer paints through distributors and retailers. In Australia and New Zealand, we sell Wattyl and Valspar brands of consumer paints through independent dealers, hardware chains, home centers and company-owned stores. In the U.K. and Ireland, we sell Valspar branded products through a large home center customer. At certain customers, we also offer additional marketing and customer support by providing Valspar personnel to train paint department employees and to answer paint questions in stores.

We develop highly customized merchandising and marketing support programs for our consumer paint customers, enabling them to differentiate their paint departments from their competitors through product and color selection assistance, point-of-purchase materials and labeling. Our primary brands include Valspar and Cabot in the U.S., Huarun in China, and Wattyl, Valspar and Solagard in Australia and New Zealand. We continue to invest in and support these brands through advertising and marketing programs.

Our automotive product line includes refinish paints and aerosol spray paints that are sold through automotive refinish distributors, body shops, automotive supply distributors and automotive supply retailers. We manufacture these products in Europe and North America and distribute them under the Valspar, DeBeer, Octoral

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and House of Kolor brands in many countries around the world.

**Other and Administrative**

In addition to the main product lines within our Coatings and Paints segments, we manufacture and sell specialty polymers and colorants, and we sell furniture protection plans and furniture care and repair products under the Guardsman brand. The specialty polymers and colorants are manufactured for internal use and for external sale to other coatings manufacturers. In the fourth quarter of fiscal year 2012, we exited the gelcoat products market.

**COMPETITION**

All aspects of the coatings and paints business are highly competitive. Some of our competitors are larger and have greater financial resources than us.

Competition in our Coatings segment is based on formulating products for specific customer applications, meeting customer delivery requirements and providing technical assistance to the customer in product application, new technology offerings and prices. We can provide global coatings solutions to customers due to our position as one of the world s largest industrial coatings manufacturers and our commitment to developing new technologies.

Competition in our Paints segment is based on factors such as consumer brand recognition, product quality, distribution and price. In this segment, we support our brand awareness through advertising and highly customized merchandising and marketing support programs provided to our customers.

**RAW MATERIALS**

We obtain raw materials from a number of suppliers. The raw materials are derived from petrochemicals, minerals and metals. Our most significant raw materials include solvents, titanium dioxide and epoxy and other resins. Historically, these materials have been generally available on the open market, with pricing and availability subject to fluctuation. Most of the raw materials used in production are purchased from outside sources. We have made, and plan to continue to make, supply arrangements to meet our current and future usage requirements. We manage sourcing of critical raw materials by establishing contracts, buying from multiple sources and identifying alternative or lower cost materials or technology, when possible. We have active initiatives to find lower cost materials, to reformulate products with lower cost and more environmentally friendly raw materials and to qualify multiple and local sources of supply, including suppliers from Asia and other lower cost regions of the world.

**INTELLECTUAL PROPERTY**

Our practice is to seek patent protection for our products and manufacturing processes when appropriate. We also license some patented technology from other sources. Our business is not materially dependent upon licenses or similar rights or on any single patent or group of related patents. Although we believe our patent rights are valuable, our knowledge and trade secret information regarding our manufacturing processes and materials have also been important in maintaining our competitive position. We require certain employees to sign confidentiality agreements relating to proprietary information.

While we make efforts to protect our trade secret information, others may independently develop or otherwise acquire substantially equivalent proprietary information or techniques or inappropriately gain access to our proprietary technology or disclose this technology. Any of these factors could adversely impact the value of our proprietary trade secret information and harm our business.

**SEASONALITY AND WORKING CAPITAL ITEMS**

Our sales volume is traditionally lowest during the first quarter of the fiscal year (November, December and January), and highest in the third quarter of the fiscal year (May, June and July), primarily due to weather and the buying cycle in our Coatings and Paints segments. When sales are lowest, we build inventory, the financing for which is provided by internally generated funds, short-term debt and long-term credit lines discussed in Note 9 of Notes to Consolidated Financial Statements.

**SIGNIFICANT CUSTOMERS**

In 2013, our sales to Lowe s Companies, Inc. exceeded 10% of consolidated net sales. Our ten largest customers accounted for approximately 33% of consolidated net sales. Our five largest customers in the Paints segment accounted for approximately 52% of our net sales in the segment. Our five largest customers in the Coatings segment accounted for approximately 19% of our net sales in the segment.

**BACKLOG AND GOVERNMENT CONTRACTS**

We have no significant backlog of orders and generally are able to fill orders on a current basis. No material portion of our business is subject to renegotiation of profits or termination of contracts or subcontracts at the election of the government.

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**RESEARCH AND DEVELOPMENT**

The base technologies that support our coatings product performance and application have been developed and optimized over many years. Our on-going applied science and development efforts are focused on delivering premium, differentiated coatings solutions that meet or exceed market needs for improved performance, consistent quality and system value. We work closely with our customers to build a deep understanding of their challenges and objectives and to foster innovation in the products and services that we provide.

Research and development costs for fiscal 2013 were $121.6 million, or 3.0% of net sales, compared to $116.9 million, or 2.9% of net sales, for fiscal 2012 and $114.6 million, or 2.9% of net sales, for fiscal 2011.

**ENVIRONMENTAL COMPLIANCE**

We undertake to comply with applicable regulations relating to protection of the environment and workers safety. Capital expenditures for this purpose were not material in fiscal 2013, and we do not expect such expenditures will be material in fiscal 2014.

**EMPLOYEES**

We employ approximately 10,700 people globally, approximately 400 of whom are subject to collective bargaining agreements in the United States. We believe that our relationship with our union employees is good.

**FOREIGN OPERATIONS AND EXPORT SALES**

Our foreign operations are conducted primarily through majority-owned subsidiaries and, to a limited extent, through joint ventures. Revenues from foreign subsidiaries and operations comprised approximately 44% of our total consolidated net sales in 2013.

In addition to our manufacturing plants in the United States, we have manufacturing plants in Australia, Brazil, Canada, China, France, Germany, India, Ireland, Italy, Malaysia, Mexico, The Netherlands, New Zealand, Poland, Singapore, South Africa, Switzerland, Thailand, the United Kingdom and Vietnam. We also have joint ventures in Japan, South Africa, Switzerland and Vietnam and sales offices in other countries.

During fiscal 2013, export sales from the United States represented 3.9% of our business.

**ITEM 1A RISK FACTORS**

*You should consider the following risk factors, in addition to the other information presented or incorporated by reference into this Annual Report on Form 10-K, in evaluating our business and your investment in us.*

***Deterioration of economic conditions could harm our business.***

Our business may be adversely affected by changes in national or global economic conditions, including inflation, interest rates, access to and the functioning of capital markets, consumer spending rates, energy availability and costs (including fuel surcharges), and the effects of governmental initiatives to manage economic conditions. Deterioration in national or global economic conditions may reduce demand for our products and overall growth of the coatings industry.

Volatility in financial markets and the deterioration of national or global economic conditions could impact our operations as follows:

- the value of our investments in debt and equity securities may decline, including our assets held in pension plans;
- the financial stability of our customers and suppliers may be compromised, which could result in additional bad debts for us or non-performance by suppliers; and
- it may become more costly or difficult to obtain financing to fund operations or investment opportunities, or to refinance our debt in the future.

At various times, we utilize hedges and other derivative financial instruments to reduce our exposure to various interest rate risks, which qualify for hedge accounting for financial reporting purposes. Volatile fluctuations in market conditions could cause these instruments to become ineffective, which could require any gains or losses associated with these instruments to be reported in our earnings each period.

***Fluctuations in the availability and prices of raw materials could negatively impact our financial results.***

We purchase the raw materials needed to manufacture our products from a number of suppliers. The majority of our raw materials are derived from petroleum, minerals and metals. Under normal market conditions, these materials are generally available from one or more suppliers on the open market. From time to time, however, the availability and costs of raw materials may fluctuate significantly, which could impair our ability to procure necessary materials, or increase the cost of manufacturing our products. Our raw material costs have been volatile, and we have experienced disruptions in supplies of certain raw materials at various times. These disruptions could affect our ability to manufacture products ordered by our customers, which could negatively impact sales.

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When raw material costs increase, our profit margins are reduced unless and until we are able to pass along the increases to our customers through higher prices. If raw material costs increase and if we are unable to pass along, or are delayed in passing along, those increases to our customers, we will experience profit margin reductions.

***Many of our customers are in cyclical industries, which may affect the demand for our products.***

Many of our customers are in businesses or industries that are cyclical and sensitive to changes in general economic conditions. As a result, the demand for our products by these customers depends, in part, upon economic cycles affecting their businesses or industries and general economic conditions. Downward economic cycles affecting the industries of our customers, and the deterioration of global economic conditions, may reduce our sales and profitability.

***The industries in which we operate are highly competitive, and some of our competitors are larger than us and may have greater financial resources than we do.***

All aspects of the coatings and paints business are highly competitive. We face strong competitors in all areas of our business. Any increase in competition may cause us to lose market share or compel us to reduce prices to remain competitive, which could result in reduced margins for our products. Competitive pressures may not only impair our margins but may also impact our revenues and our growth. A number of our competitors are larger than us and may have greater financial resources than we do. Competition with these companies could curtail price increases or require price reductions or increased spending on marketing, sales and research and development, any of which could adversely affect our results of operations.

Industry sources estimate that the top ten largest coatings manufacturers represent more than half of the world s coatings sales. Our larger competitors may have more resources to finance acquisitions or internal growth in this competitive environment. Also, we buy our raw materials from large suppliers, primarily chemical companies. In many of our product lines, we then sell our finished goods to large customers, such as do-it-yourself home centers, large equipment manufacturers and can makers. Our larger competitors may have more resources or capabilities to conduct business with these large suppliers and large customers. Finally, many of our larger competitors operate businesses in addition to paints and coatings. These competitors may be better able to compete during coatings industry downturns.

***We have a significant amount of debt.***

Our total long-term and short-term debt was $1,478.6 million at October 25, 2013. Our debt categorized as short-term was $441.2 million at October 25, 2013. Our level of debt may have important consequences. For example, it:

- may require us to dedicate a material portion of our cash flow from operations to make payments on our indebtedness, thereby reducing our ability to fund working capital, capital expenditures or other general corporate purposes;
- could make us less attractive to prospective or existing customers or less able to fund potential acquisitions; and
- may limit our flexibility to adjust to changing business and market conditions and make us more vulnerable to a downturn in general economic conditions as compared to a competitor that may have less indebtedness.

***Acquisitions are an important part of our growth strategy, and future acquisitions may not be available or successful.***

Acquisitions have historically contributed significantly to the growth of our company. As part of our growth strategy, we intend to continue to pursue acquisitions of complementary businesses and products. If we are not able to identify and complete future acquisitions, our growth may be negatively affected. Even if we are successful in completing future acquisitions, we may experience:

- difficulties in assimilating acquired companies and products into our existing business;
- delays in realizing the benefits from the acquired companies or products;
- difficulties due to lack of or limited prior experience in any new markets we may enter;
- unforeseen claims and liabilities, including unexpected environmental exposures or product liability;

unforeseen adjustments, charges and write-offs;

unexpected losses of customers of, or suppliers to, acquired businesses;

difficulty in conforming the acquired business standards, processes, procedures and controls with our operations;

variability in financial information arising from the application of purchase price accounting;

difficulties in retaining key employees of the acquired businesses; and

challenges arising from the increased geographic diversity and complexity of our operations.

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Any of these factors may make it more difficult to repay our debt or have an adverse effect on results of operations. In addition, an acquisition could materially impair our operating results by causing us to incur debt or requiring us to amortize acquisition-related costs or the cost of acquired assets.

***We derive a substantial portion of our revenues from foreign markets, which subjects us to additional business risks.***

We conduct a substantial portion of our business outside of the United States. We currently have production facilities, research and development facilities, and administrative and sales offices located outside the United States, including facilities and offices located in Australia, Brazil, Canada, China, Finland, France, Germany, Greece, India, Indonesia, Ireland, Italy, Japan, Malaysia, Mexico, The Netherlands, New Zealand, Poland, Russia, Singapore, South Africa, Spain, Switzerland, Thailand, the United Arab Emirates, the United Kingdom and Vietnam. In 2013, revenues from products sold outside the United States accounted for approximately 44% of our consolidated net sales.

We expect sales in international markets to represent a significant portion of our consolidated net sales. Notwithstanding the benefits of geographic diversification, our ability to achieve and maintain profitable growth in international markets is subject to risks related to the differing legal, political, social and regulatory requirements and economic conditions of many jurisdictions. Risks inherent in international operations include the following:

- agreements may be difficult to enforce, and receivables may be difficult to collect or have longer payment cycles;
- foreign countries may impose additional withholding taxes or otherwise tax our foreign income, or adopt other restrictions on foreign trade or investment, including currency exchange controls;
- foreign operations may experience labor disputes and difficulties in attracting and retaining key employees;
- transportation and other shipping costs may increase;
- foreign governments may nationalize private enterprises;
- unexpected adverse changes may occur in export duties, quotas and tariffs and difficulties in obtaining export licenses;
- intellectual property rights may be more difficult to enforce;
- fluctuations in exchange rates may affect product demand and may adversely affect the profitability in U.S. dollars of products and services we provide in international markets where payment for our products and services is made in the local currency;
- our business and profitability in a particular country could be affected by political or economic changes or terrorist activities and responses to such activities;
- unexpected adverse changes in foreign laws or regulatory requirements may occur; and
- compliance with a variety of foreign laws and regulations may be burdensome.

***We have certain key customers, and the loss of key customers could negatively affect our business.***

Our relationships with certain key customers are important to us. From 2011 through 2013, sales to our largest customer exceeded 10% of our consolidated net sales. In 2013, our ten largest customers accounted for approximately 33% of our consolidated net sales. Although we sell various types of products through various channels of distribution, we believe that the loss of a substantial portion of net sales to our largest customers could have a material adverse impact on us.

***If the reputation of our company or one or more of its key brands is damaged, it could harm our business.***

Our reputation is one of the foundations of our relationships with key customers and other stakeholders. If we are unable to effectively manage real or perceived issues that negatively affect our reputation, our ability to conduct our business could be impaired, and our financial results could suffer. As we continue to invest in advertising and promotion for our key brands, our financial success is becoming more dependent on the success of our brands. The success of these brands could suffer if our marketing plans or product initiatives do not have the desired effect on a brand s image, reputation or ability to attract customers. Further, our growth and results could be harmed if the reputation of our company or a key brand is damaged due to real or perceived quality issues, product recalls, regulatory enforcement or actions or customer claims and litigation.

***Technology changes, and our ability to protect our technology, could affect our business.***

Our product and application technology is supported by underlying chemistry that has been developed over many years. Ongoing research and development efforts focus on improving our internally developed and acquired technology and formulating changes to improve the performance, profitability and cost competitiveness of our products. If our competitors develop new technology, or if our customers technology requirements change, and we are not able to develop competitive technology, our business and financial results could suffer. Further, although we seek to protect

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our proprietary technology and information through confidentiality and trade secret protection programs and practices, patents, cybersecurity measures and other means, if we were unable to protect our material proprietary technology or information, our business and financial results could suffer.

***Interruption, failure or compromise of our information systems could adversely affect our business.***

We rely on information systems to run most aspects of our business, including sales and distribution of products, purchases of raw materials and supplies, accounting for purchase and sale transactions, manufacturing processes, billing and collections, and managing data and records for employees and other parties. Our business may be adversely affected if these systems are interrupted, damaged, or compromised, or if they fail for any extended period of time, due to user errors, programming errors, computer viruses, security breaches or other problems. Information security risks have generally increased in recent years because of the proliferation of new technologies and the increased sophistication and activities of cyber attackers. Although we strive to have appropriate security controls in place, prevention of security breaches cannot be assured, particularly as cyber threats continue to evolve. We may be required to expend additional resources to continue to enhance our security measures or to investigate and remediate any security vulnerabilities. In addition, third-party service providers manage a portion of our information systems, and we are subject to risk as a result of interruption, failure or security breaches of those systems. The consequences of these risks could adversely impact our results of operations and cash flows.

***Numerous laws and regulations affect our business.***

We are subject to numerous laws and regulations that control the manufacturing, marketing, sale, use and disposal of our products. These laws and regulations include health, safety, product liability, environmental and labeling requirements applicable to our products and business.

Environmental laws and regulations control, among other things, the discharge of pollutants into the air and water, the handling, use, treatment, storage and clean-up of hazardous and non-hazardous wastes, the investigation and remediation of soil and groundwater affected by hazardous substances, or otherwise relating to environmental protection and various health and safety matters. These environmental laws and regulations impose strict, retroactive and joint and several liability for the costs of, and damages resulting from, cleaning up current sites, past spills, disposals and other releases of hazardous substances and violations of these laws and regulations can also result in fines and penalties. We are currently undertaking remedial activities at a number of our facilities and properties, and have received notices under the Comprehensive Environmental Response, Compensation and Liability Act, or CERCLA, or analogous state laws, of liability or potential liability in connection with the disposal of material from our operations or former operations. Pursuant to health, safety, product liability and labeling laws and regulations, we have also been subject to various governmental enforcement actions and litigation by individuals relating to the sale, use of or exposure to our products or materials used or contained in our products, including claims for property damage or personal injury claimed to have been caused by our products or materials used or contained in our products.

We are subject to the risk that adverse decisions relating to our compliance with existing laws and regulations and new laws or regulations, or changes in existing laws or regulations or their interpretation, could increase our compliance costs and expand our potential liability for enforcement actions by governmental authorities and litigation by individuals.

In addition, our customers or consumers perceptions about the acceptability or potential environmental or health effects of certain substances could require us to invest additional amounts to develop products that exclude those substances. If we are unable to develop products that exclude those substances when and if required by our customers, we may experience reduced sales and profitability.

## ITEM 1B UNRESOLVED STAFF COMMENTS

Not applicable.

## ITEM 2 PROPERTIES

We lease our principal offices located in Minneapolis, Minnesota. Our North American manufacturing operations are conducted at 26 locations (24 owned; 2 leased) in the United States, Canada and Mexico. The total combined square footage for our principal offices and manufacturing operations in North America is approximately 4,367,000. Asia Pacific manufacturing operations are conducted at 15 locations (12 owned; 3 leased) in Australia, China, Malaysia, New Zealand, Singapore, Thailand and Vietnam, with a total combined square footage of approximately 1,995,000. European manufacturing operations are conducted at thirteen locations (10 owned; 3 leased) in France, Germany, Ireland, The Netherlands, Switzerland, Poland, Italy, and the United Kingdom, with a total combined square footage of approximately 1,403,000. In South

America, we own two manufacturing facilities in Brazil with square footage of approximately 468,000. In India, we own one manufacturing facility with square footage of approximately 121,000. In South Africa, we own one manufacturing facility with square footage of approximately 54,000.

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Shown below is a breakdown of the approximate square footage of principal facilities by region as of October 25, 2013:

| **Region** | **Approximate Square Footage Owned** | **Approximate Square Footage Leased** | **Total** |
|---|---|---|---|
| North America | 3,844,000 | 523,000 | 4,367,000 |
| Asia Pacific | 1,887,000 | 108,000 | 1,995,000 |
| Europe | 1,204,000 | 199,000 | 1,403,000 |
| Other | 643,000 | | 643,000 |
| **Total** | **7,578,000** | **830,000** | **8,408,000** |

Set forth below is a breakdown of principal facilities square footage by business segment:

| **Business Segment** | **Approximate Square Footage** |
|---|---|
| Coatings | 4,138,000 |
| Paints | 3,443,000 |
| Other and Administrative | 827,000 |
| **Total** | **8,408,000** |

We believe our manufacturing properties are well maintained, in good operating condition and adequate for the purposes for which they are being used. Operating capacity varies by product line, but additional production capacity is available for most product lines by increasing the number of days and/or shifts worked.

## ITEM 3 LEGAL PROCEEDINGS

**Environmental Matters**

We are involved in various claims relating to environmental matters at a number of current and former plant sites and waste and management sites. We engage or participate in remedial and other environmental compliance activities at certain of these sites. At other sites, we have been named as a potentially responsible party ( PRP ) under federal and state environmental laws for site remediation. We analyze each individual site, considering the number of parties involved, the level of our potential liability or contribution relative to the other parties, the nature and magnitude of the hazardous wastes involved, the method and extent of remediation, the potential insurance coverage, the estimated legal and consulting expense with respect to each site and the time period over which any costs would likely be incurred. Based on the above analysis, we estimate the clean-up costs and related claims for each site. The estimates are based in part on discussion with other PRPs, governmental agencies and engineering firms.

We accrue appropriate reserves for potential environmental liabilities, which are reviewed and adjusted as additional information becomes available. While uncertainties exist with respect to the amounts and timing of our ultimate environmental liabilities, management believes it is neither probable nor reasonably possible that such liabilities, individually or in the aggregate, will have a material adverse effect on our financial condition, results of operations or cash flows.

**Other Legal Matters**

We are involved in a variety of legal claims and proceedings relating to personal injury, product liability, warranties, customer contracts, employment, trade practices, environmental and other legal matters that arise in the normal course of business. These claims and proceedings include cases where we are one of a number of defendants in proceedings alleging that the plaintiffs suffered injuries or contracted diseases from exposure to chemicals or other ingredients used in the production of some of our products or waste disposal. We are also subject to claims related to the performance of our products. We believe these claims and proceedings are in the ordinary course for a business of the type and size in which we are engaged. While we are unable to predict the ultimate outcome of these claims and proceedings, we believe it is neither probable nor reasonably possible that the costs and liabilities of such matters, individually or in the aggregate, will have a material adverse effect on our financial condition, results of operations or cash flows.

## ITEM 4 MINE SAFETY DISCLOSURES

Not applicable.

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**EXECUTIVE OFFICERS OF THE REGISTRANT**

The names and ages of all of our executive officers, all of whom are approved by the Board of Directors for re-election in February of each year, and the positions held by them are as listed below. There are no family relationships between any of the officers or between any officer and director.

| Name | Age | Position |
|---|---|---|
| Gary E. Hendrickson | 57 | Chairman since June 2012, Chief Executive Officer since June 2011 and President and Chief Operating Officer since February 2008 |
| James L. Muehlbauer | 52 | Executive Vice President and Chief Financial and Administrative Officer since March 2013 |
| Rolf Engh | 60 | Executive Vice President since July 2005, General Counsel and Secretary since April 1993 |
| Anthony L. Blaine | 46 | Senior Vice President Human Resources since January 2007 |
| Cynthia A. Arnold | 56 | Senior Vice President and Chief Technology Officer since January 2011 |

The foregoing executive officers have served in the stated capacity for the registrant during the past five years, except for the following:

Prior to March 2013, Mr. Muehlbauer was Executive Vice President and Chief Financial Officer at Best Buy Co., Inc. since April 2008.

Prior to January 2011, Ms. Arnold was Chief Technology Officer at Sun Chemical Corporation since July 2004.

## PART II

## ITEM 5 MARKET FOR REGISTRANT S COMMONEQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our Common Stock is listed on the New York Stock Exchange under the trading symbol VAL. The table below sets forth the quarterly high and low market prices of the Common Stock for fiscal years 2013 and 2012 as quoted on the New York Stock Exchange.

| | Market Price (high/low) | | | | | |
|---|---|---|---|---|---|---|
| **For the Fiscal Year** | | **2013** | | | **2012** | |
| First Quarter | **$** | **68.42** | **55.17** | $ | 43.40 | 33.17 |
| Second Quarter | **$** | **68.30** | **58.97** | $ | 52.12 | 42.50 |
| Third Quarter | **$** | **74.25** | **62.32** | $ | 53.75 | 45.29 |
| Fourth Quarter | **$** | **71.32** | **61.13** | $ | 59.81 | 48.05 |

The quarterly dividend declared November 19, 2013, to be paid on December 13, 2013 to common stockholders of record December 2, 2013, was increased to $0.26 per share. The table below sets forth the quarterly dividends paid for fiscal years 2013 and 2012.

| | Per Share Dividends | | | |
|---|---|---|---|---|
| **For the Fiscal Year** | | **2013** | | **2012** |
| First Quarter | **$** | **0.23** | $ | 0.20 |
| Second Quarter | **$** | **0.23** | $ | 0.20 |
| Third Quarter | **$** | **0.23** | $ | 0.20 |
| Fourth Quarter | **$** | **0.23** | $ | 0.20 |
| | **$** | **0.92** | $ | 0.80 |

The number of record holders of our Common Stock at December 10, 2013 was 1,276.

**ISSUER PURCHASES OF EQUITY SECURITIES**

| Period | Total Number of Shares | Average Price Paid | Total Number of Shares Purchased as | Maximum Number of Shares that May |
|---|---|---|---|---|

| | Purchased[1] | | per Share | Part of Publicly Announced Plans or Programs[1] | Yet be Purchased Under the Plans or Programs[1] |
|---|---|---|---|---|---|
| 7/27/13 8/23/13 | | | | | |
| Repurchase program | 404,100 | $ | 66.45 | 404,100 | 10,894,600 |
| Other transactions[2] | 2,891 | $ | 69.92 | | |
| 8/24/13 9/20/13 | | | | | |
| Repurchase program | 530,000 | | 63.50 | 530,000 | 10,364,600 |
| 9/21/13 10/25/13 | | | | | |
| Repurchase program | 640,045 | | 64.97 | 640,045 | 9,724,555 |

1 On December 5, 2012, the board approved a new share repurchase authorization of 15,000,000 shares, with no predetermined end date, which replaced the October 13, 2010 authorization. In fiscal 2013 we repurchased 5,889,945 shares (5,275,445 shares under the new authorization and 614,500 under the 2010 authorization).

2 Other transactions include our acquisition of common stock in satisfaction of tax-payment obligations upon vesting of restricted stock and our receipt of surrendered shares in connection with the exercise of stock options.

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**Stock Performance Graph**

The following graph compares our cumulative total shareholder return for the last five fiscal years with the cumulative total return of the Standard & Poor s 500 Stock Index and a peer group of companies selected by us on a line-of-business basis. The graph assumes the investment of $100 in our Common Stock, the S&P 500 Index and the peer group at the end of fiscal 2008 and the reinvestment of all dividends.

The companies selected to form the peer group index are: Akzo Nobel N.V.; Ferro Corporation; H.B. Fuller Company; Masco Corporation; Newell Rubbermaid Inc.; PPG Industries, Inc.; RPM International Inc. and The Sherwin-Williams Company.

**COMPARISON OF FIVE YEAR CUMULATIVE TOTAL RETURN**
**Among The Valspar Corporation, a Peer Group and the S&P 500 Index**

| | Cumulative Total Return | | | | | |
|---|---|---|---|---|---|---|
| **Fiscal Year End** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** |
| Valspar | $ 100 | $ 128 | $ 165 | $ 188 | $ 293 | $ 380 |
| Peer Group | $ 100 | $ 122 | $ 146 | $ 154 | $ 200 | $ 297 |
| S&P 500 | $ 100 | $ 110 | $ 128 | $ 142 | $ 159 | $ 203 |

Assumes $100 invested on October 31, 2008 in the Common Stock of The Valspar Corporation, the Peer Group and the S&P 500 Index, including reinvestment of dividends.

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## ITEM 6 SELECTED FINANCIAL DATA

The following selected financial data has been derived from our audited Consolidated Financial Statements and should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and the Consolidated Financial Statements and related notes included elsewhere in this Form 10-K.

| | | Fiscal Years | | | | |
|---|---|---|---|---|---|---|
| **(Dollars in thousands, except per share amounts)** | | **2013** | **2012** | **2011** | **2010** | **2009** |
| Operating Results | Net Sales | **$ 4,103,776** | $ 4,020,851 | $ 3,952,954 | $ 3,226,687 | $ 2,879,042 |
| | Cost and Expenses | | | | | |
| | Cost of Sales | **2,745,718** | 2,667,147 | 2,721,146 | 2,155,009 | 1,900,114 |
| | Operating Expense | **865,634** | 871,434 | 862,160 | 695,601 | 687,960 |
| | Impairment of Goodwill and Intangible Assets | | | 409,714 | | |
| | Income (Loss) from Operations | **492,424** | 482,270 | (40,066) | 376,077 | 290,968 |
| | Interest Expense | **64,758** | 67,604 | 61,511 | 58,267 | 50,394 |
| | Other (Income) Expense Net | **3,871** | (2,558) | 1,577 | (1,387) | 2,246 |
| | Income (Loss) Before Income Taxes | **423,795** | 417,224 | (103,154) | 319,197 | 238,328 |
| | Net Income (Loss) | **289,255** | 292,497 | (138,601) | 222,056 | 160,153 |
| | Net Income as a Percent of Sales | **7.0%** | 7.3% | N/A | 6.9% | 5.6% |
| | Return on Average Equity | **24.7%** | 24.0% | N/A | 14.2% | 10.8% |
| | Per Common Share: | | | | | |
| | Net Income (Loss) Basic | **$ 3.29** | $ 3.20 | $ (1.47) | $ 2.25 | $ 1.50 |
| | Net Income (Loss) Diluted[1] | **3.20** | 3.10 | (1.47) | 2.20 | 1.49 |
| | Dividends Paid | **0.92** | 0.80 | 0.72 | 0.64 | 0.60 |
| Financial Position | Total Assets | **$ 4,025,509** | $ 3,626,836 | $ 3,500,151 | $ 3,867,936 | $ 3,511,024 |
| | Working Capital[2] | **591,591** | 538,559 | 538,025 | 530,435 | 406,638 |
| | Property, Plant and Equipment, Net | **633,475** | 550,968 | 548,253 | 567,630 | 471,088 |
| | Long-Term Debt, Net of Current Portion | **1,037,392** | 1,012,578 | 679,805 | 943,216 | 873,095 |
| | Stockholders Equity | **1,122,550** | 1,223,523 | 1,212,550 | 1,630,365 | 1,504,507 |
| Other Statistics | Property, Plant and Equipment Expenditures | **$ 116,749** | $ 89,363 | $ 66,469 | $ 67,732 | $ 57,897 |
| | Depreciation and Amortization Expense | **88,159** | 93,704 | 97,747 | 81,312 | 82,862 |
| | Research and Development Expense | **121,563** | 116,866 | 114,554 | 100,236 | 91,303 |
| | Total Cash Dividends | **$ 81,189** | $ 73,351 | $ 68,164 | $ 63,279 | $ 60,116 |
| | Average Diluted Common Shares Outstanding (000 s) | **90,526** | 94,380 | 94,310 | 100,866 | 100,921 |
| | Number of Stockholders at Year End | **1,290** | 1,365 | 1,405 | 1,432 | 1,449 |
| | Number of Employees at Year End | **10,702** | 9,755 | 10,020 | 10,180 | 8,788 |
| | Market Price Range Common Stock: | | | | | |
| | High | **$ 74.25** | $ 59.81 | $ 40.60 | $ 33.13 | $ 28.60 |
| | Low | **55.17** | 33.17 | 27.44 | 25.11 | 14.47 |

Reference is made to the Notes to Consolidated Financial Statements for a summary of accounting policies and additional information.

1 In 2013, 2012, 2011, 2010 and 2009, net income (loss) per common share diluted includes $0.32, $0.18, $0.24, $0.08 and $0.18 per share in restructuring charges, respectively. See Note 18 in Notes to Consolidated Financial Statements for more information on 2013, 2012 and 2011. Net income (loss) per

common share diluted for 2011 includes an impairment charge on goodwill and intangible assets of $3.75. See Management s Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Estimates and Note 1 in Notes to Consolidated Financial Statements for more information. In 2013, 2011 and 2010, net income (loss) per common share diluted includes $0.02, $0.09 and $0.03 in acquisition-related charges, respectively. Net income (loss) per common share diluted in 2010 includes gains on sale of certain assets of $0.08. Huarun Redeemable Stock accrual reduced net income (loss) per common share diluted by $0.10 in 2009. The accrual was related to our minority interest shares of Huarun Paints Holding Company Limited. Adjusted net income per common share diluted, excluding the items mentioned above, was $3.54 for 2013, $3.28 for 2012, and $2.65 for 2011, which includes a dilutive share impact of $0.04, $2.23 for 2010, and $1.77 for 2009. See related reconciliation in Management s Discussion and Analysis of Financial Condition and Results of Operations Non-GAAP Financial Measures for more information on 2013 and 2012.

[2] Working Capital is defined as accounts and notes receivable plus inventory less trade accounts payable.

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## ITEM 7 MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Dollars in thousands, except per share amounts)

Management s Discussion and Analysis of Financial Condition and Results of Operations (MD&A) is intended to provide a reader of our financial statements with a narrative from the perspective of management on our financial condition, results of operations, liquidity and certain other factors that may affect our future results. Unless otherwise noted, transactions, trends and other factors significantly impacting our financial condition, results of operations and liquidity are discussed in order of magnitude. In addition, unless expressly stated otherwise, the comparisons presented in this MD&A refer to the same period in the prior year. Our MD&A is presented in eight sections:

- Overview
- Global Economic and Industry-Wide Factors
- Results of Operations
- Financial Condition
- Non-GAAP Financial Measures
- Critical Accounting Estimates
- Off-Balance Sheet Arrangements
- Forward-Looking Statements

Our MD&A should be read in conjunction with the Consolidated Financial Statements and related Notes included in Item 8, Financial Statements and Supplementary Data, of this Form 10-K.

**OVERVIEW**

The Valspar Corporation is a global leader in the paint and coatings industry. Our strong consumer brands and leading technologies, together with our technical expertise and customer service, differentiate us from our competition and allow us to grow and create value with customers in a wide variety of geographic and end-use markets. We operate our business in two reportable segments: Coatings and Paints. Our Coatings segment aggregates our industrial product lines and our packaging product line. Our Paints segment aggregates our consumer paints and automotive refinish product lines. See Note 15 in Notes to Consolidated Financial Statements for further information on our reportable segments.

We operate in over 25 countries, and approximately 44% of our total net sales in 2013 were generated outside of the U.S. In the discussions of our operating results, we sometimes refer to the impact of changes in foreign currency exchange rates or the impact of foreign currency exchange rate fluctuations, which are references to the differences between the foreign currency exchange rates we use to convert international operating results from local currencies into U.S. dollars for reporting purposes. The impact of foreign currency exchange rate fluctuations is calculated as the difference between current period activity translated using the current period s currency exchange rates and the comparable prior-year period s currency exchange rates. We use this method to calculate the impact of changes in foreign currency exchange rates for all countries where the functional currency is not the U.S. dollar.

Our fundamental business objective is to create long-term value for our shareholders. We intend to accomplish this by:

- focusing on our customers and delivering coatings products and solutions based on a deep understanding of their needs;
- investing in our brands and developing innovative, proprietary technologies;
- expanding our global presence;

- enhancing the productivity of our business by maximizing efficiencies in procurement, manufacturing and process adherence;
- maintaining operational discipline and prudent cost control;
- generating strong cash flow; and
- allocating our capital to maintain and grow the business, fund internal growth initiatives and strategic acquisitions and pay dividends.

In addition to creating value for our shareholders, we are committed to:

- adhering to our values, ethical business conduct and doing business with integrity;
- improving the safety and reducing the environmental footprint of our business and the products we manufacture while also delivering solutions that enable our customers to meet their environmental and safety objectives; and
- demonstrating our corporate citizenship by supporting the communities in which we work and live through volunteer efforts and philanthropy.

The following discussion of financial condition and results of operations should be read in the context of this overview.

**General Economic and Industry-Wide Factors**

In North America, many of the markets in which we compete continued to improve, particularly those related to residential construction. Outside North America, we experienced softening demand, particularly in Europe, Australia and Asia. Demand in Latin America continued to grow, but at a slower rate than prior years.

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Raw material costs increased significantly in 2011 and through part of 2012. These costs moderated in the second half of 2012 and remainded stable throughout 2013. Since our raw material costs average approximately 80% of our cost of goods sold, the efficient use of raw materials is a critical cost component of the products we manufacture.

Despite the challenging global economic conditions, we continued to make solid progress on our long-term growth initiatives. In particular:

- We completed the acquisition of Inver Holdings S.r.l. (Inver Group) and the paint manufacturing business of Ace Hardware (Ace paints). The Inver Group acquisition expanded our presence in the European coatings market. As a result of the Ace paints acquisition, we expect to offer Valspar branded paints in more than 3,000 Ace retail locations in the United States.
- We won new business across all significant product lines, particularly in our consumer paints business where we made substantial gains with our professional paint product lines.
- We increased our capability to develop new technology by expanding our R&D centers in Minneapolis and China.
- We continued our initiatives to enhance productivity on a permanent basis across our operations including additional restructuring actions to improve our overall cost structure.
- We returned cash to shareholders by increasing our annual dividend 15.0% to $0.92 per share in fiscal year 2013, our 35th consecutive year with a dividend increase, and by repurchasing 5,889,945 shares for $378,141.

**Results of Operations**

*Overview*

Net sales in 2013 increased 2.1% to $4,103,776 from $4,020,851 in 2012, primarily due to new business across all significant product lines and regions and our Ace paints and Inver Group acquisitions, partially offset by volume declines in our general industrial product line and weakness in our Australia and China paints businesses. Our gross profit rate of 33.1% decreased from 33.7% in the prior year. Net income as a percent of sales of 7.0% was flat compared to last year. In 2013, we made investments in strategic acquisitions, which had lower initial margins, and invested in long-term growth initiatives. Additionally, restructuring charges increased due to current year initiatives. These costs were offset by slightly lower raw material costs and lower incentive compensation costs.

During the 2013 fiscal year, we generated $200,566 in free cash flow (defined as net cash provided by operating activities of $398,504, less capital expenditures and dividends), an increase of $14,412 from the prior year due to improved operating results, partially offset by increased investments in capital expenditures and increased dividends. We believe this non-GAAP measure (free cash flow) provides useful information to both management and investors by including the amount reinvested in the business for capital expenditures and the return on investment to our shareholders through payment of dividends. Our total debt of $1,478,557 increased by $327,448 due to our share repurchases, debt used to finance acquisitions and capital expenditures, partially offset by operating cash flow and option exercise proceeds. In July 2013, we entered into a U.S. dollar equivalent unsecured committed revolving bilateral credit facility, expiring July 2014 with total capacity of $107,767, which was used to partially finance the Inver Group acquisition. Our liquidity position is strong, with $216,150 in cash and cash equivalents and $427,517 in unused committed bank credit facilities providing total committed liquidity of $643,667 compared to $760,655 at the end of 2012.

*Restructuring*

Fiscal year 2013 restructuring initiatives included the following: (i) actions in the Paints segment to consolidate manufacturing and distribution operations following the acquisition of Ace Hardware Corporation s paint manufacturing business, ongoing profit improvement plans in Australia, and other actions in Asia, (ii) actions in our Coatings segment to consolidate manufacturing operations in Europe following the acquisition of the Inver Group, and other actions to rationalize manufacturing operations and lower operating expenses, and (iii) overall initiatives to improve our global cost structure, including non-manufacturing headcount reductions. We expect the majority of the restructuring activities commenced in fiscal year 2013 to be completed by the end of fiscal year 2014. These restructuring activities resulted in pre-tax charges of $36,433 or $0.32 per share in fiscal year 2013, and we expect the total pre-tax cost of all restructuring activities to be approximately $68,000 to $74,000 or $0.59 to $0.64 per share in 2013 and 2014. Included in fiscal year 2013 restructuring charges is $6,664 of non-cash pre-tax asset impairment charges. Subsequent to the end of the fiscal year and prior to filing this report, we incurred approximately $12,000 in pre-tax restructuring charges related to the continuation of these actions. See Note 2 in Notes to Consolidated Financial Statements for further information on our Inver Group acquisition and Note 18 in Notes to Consolidated Financial Statements for further information on restructuring. See reconciliation in Management s Discussion and Analysis of Financial Condition and Results of Operations Non-GAAP Financial Measures for more information on the per share impact of restructuring charges.

In fiscal year 2012, we exited the gelcoat products market and consolidated a manufacturing facility in our Paints segment. Our gelcoat product line was categorized in Other and Administrative. During fiscal year 2012, we also completed restructuring initiatives announced in 2011, including certain actions in our Coatings and Paints segments. In our Coatings segment,

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we rationalized our manufacturing capacity and reduced our overall global headcount, primarily in our wood product line. In our Paints segment, we completed the first phase of actions to improve the profitability of our Australian operations, which included facility consolidations in manufacturing and distribution, store rationalization and the reduction of other related costs. These restructuring activities resulted in pre-tax charges of $25,845 or $0.18 per share in fiscal year 2012.

*Vendor Support Program Change*

We provide our customers a number of cooperative marketing and trade promotional programs (vendor support programs). Our consumer directed and specifically identifiable cooperative marketing programs and activities are recorded in operating expense, and our trade promotional funding is recorded as a reduction to net sales. In 2013, the agreement with respect to cooperative advertising programs with a large customer in our Paints segment was changed. These programs are now included as reduction in price. Previously, these programs were specifically identifiable and included in operating expense. As a result, compared to last year, our net sales, gross margins and operating expenses are lower. There was no impact on net income for the change in our vendor support programs.

*Financial Results 2013 vs. 2012*

The following tables present selected financial data for the years ended October 25, 2013 and October 26, 2012.

| **Net Sales** | **2013** | **2012** | **% Change** |
|---|---|---|---|
| Coatings | **$ 2,209,492** | $ 2,175,687 | 1.6% |
| Paints | **1,671,228** | 1,604,599 | 4.2% |
| Other and Administrative | **223,056** | 240,565 | (7.3)% |
| Consolidated Net Sales | **$ 4,103,776** | $ 4,020,851 | 2.1% |

**Consolidated Net Sales** Consolidated net sales for the year increased 2.1%, including a positive impact of 2.4% from acquisitions and a negative impact of 0.5% from foreign currency. The remaining increase in sales of 0.2% was due to new business across all significant product lines and regions. The increase was partially offset by volume declines caused by continued weakness in our global general industrial product line, a weak residential housing market in Australia and lower sales in our China consumer paints product line.

**Coatings Segment Net Sales** Our Coatings segment net sales for the year increased 1.6%, including a positive impact of 1.4% from acquisitions and a negative impact of 0.6% from foreign currency. The remaining increase in sales of 0.8% was primarily due to volume growth driven by new business in all significant product lines, which was partially offset by continued weakness in our general industrial product line.

**Paints Segment Net Sales** Our Paints segment net sales for the year increased 4.2%, including a positive impact of 4.2% from acquisitions and a negative impact of 0.3% from foreign currency. The remaining increase in sales of 0.3% reflects new business in our North America consumer paints market, partially offset by declines in international consumer markets due to a weak residential housing market in Australia and lower sales in China.

**Other and Administrative Net Sales** The Other and Administrative category includes the following product lines: resins, furniture protection plans, colorants and gelcoats. Other and Administrative net sales decreased 7.3%, including a negative impact of 0.1% from foreign currency. The decline was primarily due to our exit from the gelcoat products market in the fourth quarter of 2012.

| **Gross Profit** | **2013** | **2012** |
|---|---|---|
| Consolidated Gross Profit | **$ 1,358,058** | $ 1,353,704 |
| As a percent of Net Sales | **33.1%** | 33.7% |

**Gross Profit** The gross profit rate decreased 0.6% primarily due to investments in strategic acquisitions, which had lower initial margins, changes in certain vendor support programs and higher restructuring charges, partially offset by slightly lower raw material costs. Restructuring charges of $21,916 or 0.5% of net sales and $16,199 or 0.4% of net sales were included in the 2013 and 2012 periods, respectively. Acquisition-related charges were $513, or 0.01% of net sales. There were no acquisition-related charges included in gross profit in the 2012 period.

| **Operating Expenses** | | **2013** | | **2012** |
|---|---|---|---|---|
| Consolidated Operating Expenses[1] | **$** | **865,634** | $ | 871,434 |
| As a percent of Net Sales | | **21.1%** | | 21.7% |

1 Includes research and development, selling, general and administrative, restructuring and acquisition-related costs. For breakout see Consolidated Statements of Operations.

**Consolidated Operating Expenses (dollars)** Consolidated operating expenses decreased 0.7% compared to the prior year primarily due to changes in certain vendor support programs in our Paints segment and lower incentive compensation, partially offset by investments to support growth initiatives in both our Paints and Coatings segments and higher restructuring charges. Restructuring charges of $14,517 or 0.4% of net sales and $9,646 or 0.2% of net sales were included in the 2013 and 2012 periods, respectively. Acquisition-related charges were $1,729, or 0.04% of net sales in 2013. There were no acquisition-related charges included in operating expenses in the 2012 period.

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| **EBIT**[1] | | **2013** | | 2012 |
|---|---|---|---|---|
| Coatings | **$** | **329,886** | $ | 356,428 |
| As a percent of Net Sales | | **14.9%** | | 16.4% |
| Paints | | **168,395** | | 159,598 |
| As a percent of Net Sales | | **10.1%** | | 9.9% |
| Other and Administrative | | **(9,728)** | | (31,198) |
| As a percent of Net Sales | | **(4.4)%** | | (13.0)% |
| Consolidated EBIT | **$** | **488,553** | $ | 484,828 |
| As a percent of Net Sales | | **11.9%** | | 12.1% |

1 EBIT is defined as earnings before interest and taxes.

**Consolidated EBIT** EBIT for 2013 increased $3,725 or 0.8% from the prior year. Fiscal year 2013 results included restructuring charges of $36,433 or 0.9% of net sales, compared to $25,845 or 0.6% of net sales in fiscal year 2012. Fiscal year 2013 also included acquisition-related charges of $2,242 or 0.1% of net sales. There were no acquisition-related charges in the 2012 period. Foreign currency exchange fluctuation had an immaterial effect on Consolidated EBIT, as well as EBIT of the segments discussed below.

**Coatings Segment EBIT** EBIT as a percent of net sales decreased 150 basis points from the prior year, primarily due to higher restructuring charges, price declines and investments in long-term growth initiatives, partially offset by slightly lower raw material costs and lower incentive compensation costs. Restructuring charges for the 2013 and 2012 periods were $19,492 or 0.9% of net sales and $1,418 or 0.1% of net sales, respectively. Acquisition-related charges were $2,242 or 0.1% of net sales. There were no acquisition-related charges in the 2012 period.

**Paints Segment EBIT** EBIT as a percent of net sales increased 20 basis points from the prior year, primarily due to slightly lower raw material costs and lower restructuring charges, partially offset by the effect of our Ace paints acquisition, which had lower initial margins, and investments in long-term growth initiatives. Restructuring charges for 2013 and 2012 periods were $14,953 or 0.9% of net sales and $18,392 or 1.1% of net sales, respectively.

**Other and Administrative EBIT** Other and Administrative EBIT includes corporate expenses. EBIT as a percent of net sales increased 860 basis points from the prior year primarily due to lower incentive compensation and lower restructuring charges. EBIT included restructuring charges of $1,988 or 0.9% of net sales and $6,035 or 2.5% of net sales in the 2013 and 2012 periods, respectively.

| **Interest Expense** | | **2013** | | 2012 |
|---|---|---|---|---|
| Consolidated Interest Expense | **$** | **64,758** | $ | 67,604 |

**Interest Expense** Interest expense decreased in fiscal year 2013 due to lower average interest rates, partially offset by a higher average debt balance. In 2013, although our average debt levels increased, a greater percentage of our debt was commercial paper, which carries a lower interest rate.

| **Effective Tax Rate** | **2013** | 2012 |
|---|---|---|
| Effective Tax Rate | **31.7%** | 29.9% |

**Effective Tax Rate** The higher 2013 effective tax rate was primarily due to unfavorable changes in geographical mix of earnings.

| Net Income (Loss) | | 2013 | | 2012 | % Change |
|---|---|---|---|---|---|
| Consolidated Net Income (Loss) | $ | **289,255** | $ | 292,497 | (1.1)% |

*Financial Results 2012 vs. 2011*

| Net Sales | | 2012 | | 2011 | % Change |
|---|---|---|---|---|---|
| Coatings | $ | **2,175,687** | $ | 2,092,490 | 4.0% |
| Paints | | **1,604,599** | | 1,612,219 | (0.5) % |
| Other and Administrative | | **240,565** | | 248,245 | (3.1)% |
| Consolidated Net Sales | $ | **4,020,851** | $ | 3,952,954 | 1.7% |

**Consolidated Net Sales** Adjusting for the negative impact of 1.3% from foreign currency and the positive impact of 0.4% from acquisitions, sales for 2012 increased 2.6%. The increase in sales was due to carryover selling price increases in all product lines and new business, primarily in our Coatings segment. The increase was partially offset by volume declines caused by uneven demand in our global markets.

**Coatings Segment Net Sales** Adjusting for the negative impact of 2.3% from foreign currency and the positive impact of 0.8% from acquisitions, sales for 2012 increased 5.5%. The increase in sales was primarily due to new business and carryover selling price increases in all product lines. The increase was partially offset by volume declines caused by our decision to exit a small number of relatively high volume, unprofitable products and customers, and overall market softness.

**Paints Segment Net Sales** Sales for 2012 decreased 0.5%. There was no net foreign currency impact. The decrease in sales was primarily driven by declines in our Australia region due to a weak residential housing market, our efforts to rationalize company stores and loss of a large retail customer. This was partially offset by higher sales volumes in our China consumer paints product line.

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**Other and Administrative Net Sales** The Other and Administrative category includes the following product lines: resins, furniture protection plans, colorants and gelcoats. Adjusting for the negative impact of 0.7% from foreign currency, sales for the 2012 period decreased 2.4%. The decline was primarily due to lower sales in the gelcoat products market which we exited in the fourth quarter of 2012.

| Gross Profit | 2012 | 2011 |
|---|---|---|
| Consolidated Gross Profit | **$ 1,353,704** | $ 1,231,808 |
| As a percent of Net Sales | **33.7%** | 31.2% |

**Gross Profit** Gross profit as a percent of net sales increased primarily due to our carryover selling price increases, productivity improvements, including savings from our previously completed restructuring actions, new business at higher average gross margins, acquisition-related charges recognized in 2011 and lower restructuring charges in 2012. The improvement was partially offset by higher raw material costs. Restructuring charges of $16,199 or 0.4% of net sales and $25,563 or 0.6% of net sales were included in the 2012 and 2011 periods, respectively. There were no acquisition-related charges included in gross profit in the 2012 period. Acquisition-related charges were $11,416 or 0.3% of net sales in the 2011 period.

| Operating Expenses | 2012 | 2011 |
|---|---|---|
| Consolidated Operating Expenses[1] | **$ 871,434** | $ 862,160 |
| As a percent of Net Sales | **21.7%** | 21.8% |

1 Includes research and development, selling, general and administrative and restructuring costs. For breakout see Consolidated Statements of Operations.

**Consolidated Operating Expenses (dollars)** Consolidated operating expenses increased 1.1% or $9,274 compared to the prior year. The increase was driven primarily by higher incentive compensation and investments in growth initiatives, partially offset by savings from previously completed restructuring initiatives. Restructuring charges of $9,646 or 0.2% of net sales and $8,876 or 0.2% of net sales were included in the 2012 and 2011 periods, respectively. There were no acquisition-related charges included in operating expenses in the 2012 period. Acquisition-related charges of $1,859 or 0.1% of net sales were included in operating expenses in the 2011 period.

| EBIT[1] | 2012 | 2011 |
|---|---|---|
| Coatings | **$ 356,428** | $ (112,209) |
| As a percent of Net Sales | **16.4%** | (5.4)% |
| Paints | **159,598** | 134,886 |
| As a percent of Net Sales | **9.9%** | 8.4% |
| Other and Administrative | **(31,198)** | (64,320) |
| As a percent of Net Sales | **(13.0)%** | (25.9)% |
| Consolidated EBIT | **$ 484,828** | $ (41,643) |
| As a percent of Net Sales | **12.1%** | (1.1)% |

1 EBIT is defined as earnings before interest and taxes

**Consolidated EBIT** EBIT for 2012 increased $526,471 from the prior year. Fiscal year 2012 includes restructuring charges of $25,845 or 0.6% of net sales. Fiscal year 2011 includes the impairment charge of $409,714 or 10.4% of net sales, restructuring charges of $34,439 or 0.9% of net sales and acquisition-related charges of $13,275 or 0.3% net sales. Foreign currency exchange fluctuation had an immaterial effect on Consolidated EBIT, as well as EBIT of the segments discussed below.

**Coatings Segment EBIT** EBIT as a percent of net sales increased primarily due to the impairment charge recognized in 2011, carryover selling price increases, productivity improvements, including savings from our previously completed restructuring actions, higher margin new business and lower restructuring charges in 2012. The increase was partially offset by higher raw material costs. The restructuring charges for 2012 and 2011 periods were $1,418 or 0.1% of net sales and $20,940 or 1.0% of net sales, respectively. There were no acquisition-related charges included in EBIT in the 2012 period. EBIT included acquisition-related charges of $1,859 or 0.1% of net sales in the 2011 period. There was no impairment charge on goodwill and intangible assets included in EBIT in the 2012 period. EBIT included an impairment charge of $368,062 or 17.6% of net sales in the 2011 period.

**Paints Segment EBIT** EBIT as a percent of net sales increased primarily due to selling price increases, productivity improvements, including savings from our previously completed restructuring actions particularly in our Australia paints product line, and acquisition-related charges recognized in the first half of 2011. These improvements were partially offset by higher raw material costs and higher restructuring charges in 2012 versus 2011. The restructuring charges for 2012 and 2011 periods were $18,392 or 1.1% of net sales and $13,013 or 0.8% of net sales, respectively. There were no acquisition-related charges included in EBIT in the 2012 period. EBIT included acquisition-related charges of $11,416 or 0.7% of net sales in the 2011 period.

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**Other and Administrative EBIT** Other and Administrative EBIT includes corporate expenses. EBIT as a percent of net sales increased compared to the prior year primarily due to the impairment charge of $41,652 or 16.8% of net sales recognized in the fourth quarter of 2011, partially offset by higher restructuring charges in the 2012 period. EBIT included restructuring charges of $6,035 or 2.5% of net sales and $486 or 0.2% of net sales in the 2012 and 2011 periods, respectively.

| Interest Expense | 2012 | 2011 |
|---|---|---|