CABOT CORP
Form 10-Q
May 07, 2015
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2015

or

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

For the transition period from __________ to __________

Commission file number 1-5667

Cabot Corporation

(Exact name of registrant as specified in its charter)

Delaware	**04-2271897**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
Two Seaport Lane	
Boston, Massachusetts	**02210-2019**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (617) 345-0100

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

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

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

Large accelerated filer x	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if smaller reporting company)	Smaller reporting company ¨

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

Indicate the number of shares outstanding of each of the issuer s classes of Common Stock, as of the latest practicable date.

As of May 4, 2015 the Company had 63,466,995 shares of Common Stock, par value $1.00 per share, outstanding.

Table of Contents

CABOT CORPORATION

INDEX

Table of Contents

Part I. Financial Information

Item 1. Financial Statements

CABOT CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS

UNAUDITED

	Three Months Ended March 31		Six Months Ended March 31	
	2015	2014	2015	2014
	(In millions, except per share amounts)			
Net sales and other operating revenues	$ 694	$ 898	$ 1,506	$ 1,796
Cost of sales	555	722	1,210	1,441
Gross profit	139	176	296	355
Selling and administrative expenses	71	92	149	169
Research and technical expenses	14	16	29	31
Income from operations	54	68	118	155
Interest and dividend income	1	1	2	2
Interest expense	(14)	(13)	(27)	(27)
Other (expense) income	(2)	(8)	(3)	27
Income from continuing operations before income taxes and equity in earnings (loss) of affiliated companies	39	48	90	157
Provision for income taxes	(14)	(7)	(17)	(31)
Equity in earnings (loss) of affiliated companies, net of tax	2	(2)	3	
Income from continuing operations	27	39	76	126
Loss from discontinued operations, net of tax				(1)
Net income	27	39	76	125
Net income attributable to noncontrolling interests, net of tax	1	3	5	9
Net income attributable to Cabot Corporation	$ 26	$ 36	$ 71	$ 116
Weighted-average common shares outstanding, in millions:				
Basic	63.6	64.4	63.9	64.2
Diluted	64.1	65.1	64.4	65.0

Income per common share:								
Basic:								
Income from continuing operations attributable to Cabot Corporation	$	0.41	$	0.56	$	1.11	$	1.81
Loss from discontinued operations				(0.01)				(0.02)
Net income attributable to Cabot Corporation	$	0.41	$	0.55	$	1.11	$	1.79
Diluted:								
Income from continuing operations attributable to Cabot Corporation	$	0.41	$	0.55	$	1.10	$	1.79
Loss from discontinued operations				(0.01)				(0.02)
Net income attributable to Cabot Corporation	$	0.41	$	0.54	$	1.10	$	1.77
Dividends per common share	$	0.22	$	0.20	$	0.44	$	0.40

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

Table of Contents

CABOT CORPORATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS) INCOME

UNAUDITED

	Three Months Ended March 31		Six Months Ended March 31	
	2015	2014	2015	2014
	(In millions)			
Net income	$ 27	$ 39	$ 76	$ 125
Other comprehensive loss, net of tax				
Foreign currency translation adjustment (net of tax provision of $-, $-, $1 and $1)	(131)	(8)	(234)	(29)
Pension and other postretirement benefit liability adjustments				
Pension and other postretirement benefit liability adjustments arising during the period (net of tax benefit of $-, $-, $6 and $-)			21	
Amortization of net loss and prior service credit included in net periodic pension cost (net of tax benefit of less than $1 million in all periods)	1	1	1	1
Other comprehensive loss	(130)	(7)	(212)	(28)
Comprehensive (loss) income	(103)	32	(136)	97
Net income attributable to noncontrolling interests	1	3	5	9
Noncontrolling interests foreign currency translation adjustment, net of tax	(1)	(1)	(3)	(2)
Comprehensive income attributable to noncontrolling interests, net of tax		2	2	7
Comprehensive (loss) income attributable to Cabot Corporation	$ (103)	$ 30	$ (138)	$ 90

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

4

Table of Contents

CABOT CORPORATION

CONSOLIDATED BALANCE SHEETS

ASSETS

UNAUDITED

	March 31, 2015	September 30, 2014
	(In millions)	
Current assets:		
Cash and cash equivalents	$ 94	$ 67
Accounts and notes receivable, net of reserve for doubtful accounts of $8 and $7	567	688
Inventories:		
Raw materials	76	111
Work in process	1	2
Finished goods	290	341
Other	41	44
Total inventories	408	498
Prepaid expenses and other current assets	63	69
Deferred income taxes	39	42
Total current assets	1,171	1,364
Property, plant and equipment, net	1,483	1,581
Goodwill	508	536
Equity affiliates	63	68
Intangible assets, net	320	347
Assets held for rent	63	56
Deferred income taxes	74	80
Other assets	50	52
Total assets	$ 3,732	$ 4,084

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

Table of Contents

CABOT CORPORATION

CONSOLIDATED BALANCE SHEETS

LIABILITIES AND STOCKHOLDERS EQUITY

UNAUDITED

	March 31, 2015	September 30, 2014
	(In millions, except share and per share amounts)	
Current liabilities:		
Notes payable	$ 133	$ 44
Accounts payable and accrued liabilities	386	512
Income taxes payable	36	49
Deferred income taxes	1	1
Current portion of long-term debt	1	24
Total current liabilities	557	630
Long-term debt	995	1,004
Deferred income taxes	63	68
Other liabilities	252	291
Redeemable preferred stock	28	27
Commitments and contingencies (Note I)		
Stockholders equity:		
Preferred stock:		
Authorized: 2,000,000 shares of $1 par value		
Issued and Outstanding : None and none		
Common stock:		
Authorized: 200,000,000 shares of $1 par value		
Issued: 63,702,325 and 64,634,731 shares		
Outstanding: 63,449,960 and 64,382,366 shares	63	64
Less cost of 252,365 and 252,365 shares of common treasury stock	(7)	(7)
Additional paid-in capital		49
Retained earnings	1,943	1,900
Accumulated other comprehensive loss	(273)	(64)
Total Cabot Corporation stockholders equity	1,726	1,942
Noncontrolling interests	111	122
Total stockholders equity	1,837	2,064
Total liabilities and stockholders equity	$ 3,732	$ 4,084

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

Table of Contents

CABOT CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

UNAUDITED

	Six Months Ended March 31 2015	Six Months Ended March 31 2014
	(In millions)	
Cash Flows from Operating Activities:		
Net income	$ 76	$ 125
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation and amortization	92	100
Impairment of assets		3
Deferred tax provision	(2)	(3)
Gain on existing investment in NHUMO		(29)
Employee benefit plan settlement	18	
Equity in earnings of affiliated companies	(3)	
Non-cash compensation	6	8
Other	(4)	
Changes in assets and liabilities:		
Accounts and notes receivable	71	(52)
Inventories	55	(76)
Prepaid expenses and other current assets		(15)
Accounts payable and accrued liabilities	(85)	(14)
Income taxes payable	(13)	1
Other liabilities	(18)	4
Cash dividends received from equity affiliates	7	21
Other	5	(4)
Cash provided by operating activities	205	69
Cash Flows from Investing Activities:		
Additions to property, plant and equipment	(70)	(70)
Change in assets held for rent	(7)	(5)
Cash paid for acquisition of business, net of cash acquired of $7		(73)
Cash used in investing activities	(77)	(148)
Cash Flows from Financing Activities:		
Borrowings under financing arrangements		13
Repayments under financing arrangements	(3)	(6)
Proceeds from long-term debt, net of issuance costs		15
Repayments of long-term debt	(32)	(7)
Decrease in notes payable, net	(1)	(5)

Proceeds from issuance of commercial paper, net	94	111
Purchases of common stock	(61)	(6)
Proceeds from sales of common stock	5	10
Cash dividends paid to noncontrolling interests	(11)	(10)
Cash dividends paid to common stockholders	(28)	(26)
Cash (used in) provided by financing activities	(37)	89
Effect of exchange rate changes on cash	(64)	(16)
Increase (Decrease) in cash and cash equivalents	27	(6)
Cash and cash equivalents at beginning of period	67	95
Cash and cash equivalents at end of period	$ 94	$ 89

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

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

A. Basis of Presentation

The consolidated financial statements include the accounts of Cabot Corporation (Cabot or the Company) and its wholly owned subsidiaries and majority-owned and controlled U.S. and non-U.S. subsidiaries. Additionally, Cabot considers consolidation of entities over which control is achieved through means other than voting rights in the periods presented. Intercompany transactions have been eliminated in consolidation.

The unaudited consolidated financial statements have been prepared in accordance with the requirements of Form 10-Q and consequently do not include all disclosures required by Form 10-K. Additional information may be obtained by referring to Cabot s Annual Report on Form 10-K for the fiscal year ended September 30, 2014 (2014 10-K).

The financial information submitted herewith is unaudited and reflects all adjustments which are, in the opinion of management, necessary to provide a fair statement of the results for the interim periods ended March 31, 2015 and 2014. All such adjustments are of a normal recurring nature. The results for interim periods are not necessarily indicative of the results to be expected for the fiscal year.

In November 2013, the Company purchased all of Grupo Kuo S.A.B. de C.V. s (KUO) common stock in NHUMO, S.A. de C.V. (NHUMO), a carbon black joint venture between the Company and KUO in Mexico, which represented approximately 60% of the outstanding common stock of NHUMO (the NHUMO transaction). Prior to this transaction, the Company owned approximately 40% of the outstanding common stock of NHUMO, and the NHUMO entity was accounted for as an equity affiliate of the Company. The financial position, results of operations and cash flows of NHUMO are included in the Company s consolidated financial statements from the date of acquisition.

In July 2014, the Company completed the sale of its Security Materials business. The Consolidated Statements of Operations and the notes to the consolidated financial statements for all periods presented exclude the Security Materials business.

In December 2014, the Company realigned its business reporting structure into four segments that consist of Reinforcement Materials, Performance Chemicals, Purification Solutions and Specialty Fluids. The new structure is aligned with senior management changes and it better leverages Cabot s global activities across common customer applications, production, and research and development activities. Prior period segment results have been recast to reflect the realignment.

B. Significant Accounting Policies

Revenue Recognition and Accounts Receivable

Cabot recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price is fixed or determinable and collectability is reasonably assured. Cabot generally is able to ensure that products meet customer specifications prior to shipment. If the Company is unable to determine that the product has met the specified objective criteria prior to shipment or if title has not transferred because of sales terms, the revenue is considered unearned and is deferred until the revenue recognition criteria are met.

Shipping and handling charges related to sales transactions are recorded as sales revenue when billed to customers or included in the sales price.

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

The following table shows the relative size of the revenue recognized in each of the Company s reportable segments for the periods presented.

	Three Months Ended March 31		Six Months Ended March 31	
	2015	2014	2015	2014
Reinforcement Materials	53%	58%	56%	59%
Performance Chemicals	35%	30%	32%	29%
Purification Solutions	11%	9%	10%	9%
Specialty Fluids	1%	3%	2%	3%

Cabot derives the substantial majority of its revenues from the sale of products in Reinforcement Materials and Performance Chemicals. Revenue from these products is typically recognized when the product is shipped and title and risk of loss have passed to the customer. The Company offers certain of its customers cash discounts and volume rebates as sales incentives. Depending on the nature of the contract with the customer, a portion of the revenue may be recognized using proportional performance. The discounts and volume rebates are recorded as a reduction in sales at the time revenue is recognized and are estimated based on historical experience and contractual obligations. Cabot periodically reviews the assumptions underlying its estimates of discounts and volume rebates and adjusts its revenues accordingly.

Revenue in Purification Solutions is typically recognized when the product is shipped and title and risk of loss have passed to the customer. For major activated carbon injection systems projects, revenue is recognized using the percentage-of-completion method.

Revenue in Specialty Fluids arises primarily from the rental of cesium formate. This revenue is recognized throughout the rental period based on the contracted rental terms. Customers are also billed and revenue is recognized, typically at the end of the job, for cesium formate product that is not returned. The Company also generates revenues from cesium formate sold outside of a rental process and revenue is recognized upon delivery of the fluid.

Cabot maintains allowances for doubtful accounts based on an assessment of the collectability of specific customer accounts, the aging of accounts receivable and other economic information on both a historical and prospective basis. Customer account balances are charged against the allowance when it is probable the receivable will not be recovered. There is no material off-balance sheet credit exposure related to customer receivable balances.

Property, Plant and Equipment

Property, plant and equipment are recorded at cost. Depreciation of property, plant and equipment is generally calculated using the straight-line method over the estimated useful lives. The depreciable lives for buildings, machinery and equipment, and other fixed assets are twenty to twenty-five years, ten to twenty-five years, and three to twenty-five years, respectively. The cost and accumulated depreciation for property, plant and equipment sold, retired, or otherwise disposed of are removed from the Consolidated Balance Sheets and resulting gains or losses are included in earnings in the Consolidated Statements of Operations. Expenditures for repairs and maintenance are charged to expenses as incurred. Expenditures for major renewals and betterments, which significantly extend the useful lives of existing plant and equipment, are capitalized and depreciated.

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

Intangible Assets and Goodwill

The Company records tangible and intangible assets acquired and liabilities assumed in business combinations under the acquisition method of accounting. Amounts paid for an acquisition are allocated to the assets acquired and liabilities assumed based on their fair values at the date of acquisition. Goodwill is comprised of the purchase price of business acquisitions in excess of the fair value assigned to the net tangible and identifiable intangible assets acquired. Goodwill is not amortized, but is reviewed for impairment annually as of May 31, or when events or changes in the business environment indicate that the carrying value of the reporting unit may exceed its fair value. A reporting unit, for the purpose of the impairment test, is at or below the operating segment level, and constitutes a business for which discrete financial information is available and regularly reviewed by segment management. The separate businesses included within Performance Chemicals are considered separate reporting units. The goodwill balance relative to this segment is recorded in the Fumed Metal Oxides reporting unit within Performance Chemicals.

For the purpose of the goodwill impairment test, the Company first assesses qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If an initial qualitative assessment identifies that it is more likely than not that the carrying value of a reporting unit exceeds its estimated fair value, an additional quantitative evaluation is performed under the two-step impairment test. Alternatively, the Company may elect to proceed directly to the quantitative goodwill impairment test. If based on the quantitative evaluation the fair value of the reporting unit is less than its carrying amount, the Company performs an analysis of the fair value of all assets and liabilities of the reporting unit. If the implied fair value of the reporting unit s goodwill is determined to be less than its carrying amount, an impairment is recognized for the difference. The fair value of a reporting unit is based on discounted estimated future cash flows. The fair value is also benchmarked against a market approach using the guideline public companies method. The assumptions used to estimate fair value include management s best estimates of future growth rates, operating cash flows, capital expenditures and discount rates over an estimate of the remaining operating period at the reporting unit level. Should the fair value of any of the Company s reporting units decline because of reduced operating performance, market declines, changes in the discount rate, or other indicators of impairment, charges for impairment may be necessary. Based on the Company s most recent annual goodwill impairment test performed as of May 31, 2014, the fair values of the Reinforcement Materials and Fumed Metal Oxides reporting units were substantially in excess of their carrying values. At that date, the fair value of the Purification Solutions reporting unit exceeded its carrying value by approximately 9%. At March 31, 2015, the Purification Solutions reporting unit had the most significant goodwill balance, in the amount of $439 million. The future growth in the Purification Solutions segment is highly dependent on achieving the expected volumes and margins in the activated carbon based mercury removal business. These volumes and margins are highly dependent on demand for mercury removal products and the Company s successful realization of its anticipated share of volumes in this segment. The expected demand for mercury removal products significantly depends on: (1) the implementation and enforcement of environmental laws and regulations, particularly those that would require U.S. based coal-fired electric utilities to reduce the quantity of air pollutants they release, including mercury, to comply with the Mercury and Air Toxics Standards (MATS) and (2) other factors such as the anticipated usage of activated carbon in the coal-fired energy units. In November 2014, the U.S. Supreme Court agreed to consider whether the Environmental Protection Agency (EPA) appropriately considered costs in determining whether it is necessary and appropriate to regulate hazardous air pollutants emitted by electric utilities, and oral arguments were heard by the Court in March 2015. It is not possible to predict the outcome of the Supreme Court s review of this matter.

The implementation period for the MATS regulations began in April 2015. With this recent implementation, as well as associated customer and industry feedback, the Company is reassessing its previous estimates for expected growth in volumes, prices and profitability in the Purification Solutions reporting unit. Potential drivers of growth, including the size of the overall mercury removal industry, utility adoption rates, usage levels, and pricing, among others, are still evolving. If the Company determines, based on these estimates, that the fair value of its Purification Solutions reporting unit is below the carrying amount, the Company may be required to record an asset impairment charge. With the evolving view of the market, the Company currently believes that it is reasonably possible that a non-cash impairment charge may be required. However, this is a preliminary view and Cabot expects to complete its analysis during the third fiscal quarter. This charge, if any, could be material and could impact goodwill, intangible assets, and long-lived assets. As of March 31, 2015, the carrying value of the Purification Solutions reporting unit was $1.1 billion, which included goodwill and intangibles in the amounts of $439 million and $270 million, respectively, and other long-lived assets.

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

The Company uses assumptions and estimates in determining the fair value of assets acquired and liabilities assumed in a business combination. The determination of the fair value of intangible assets requires the use of significant judgment with regard to assumptions used in the valuation model. The Company estimates the fair value of identifiable acquisition-related intangible assets principally based on projections of cash flows that will arise from these assets. The projected cash flows are discounted to determine the fair value of the assets at the dates of acquisition.

Definite-lived intangible assets, which are comprised of customer relationships and developed technologies, are amortized over their estimated useful lives and are reviewed for impairment when indication of potential impairment exists, such as a significant reduction in cash flows associated with the assets. The Company evaluates indefinite-lived intangible assets, which are comprised of the trademarks of Purification Solutions, for impairment annually or when events occur or circumstances change that may reduce the fair value of the asset below its carrying amount. The annual review is performed as of May 31. The Company may first perform a qualitative assessment to determine whether it is necessary to perform the quantitative impairment test or bypass the qualitative assessment and proceed directly to performing the quantitative impairment test. The quantitative impairment test is based on discounted estimated future cash flows. The assumptions used to estimate fair value include management s best estimates of future growth rates and discount rates over an estimate of the remaining operating period at the unit of accounting level. These future growth rates depend on achieving the expected volumes and pricing levels of the products of Purification Solutions.

Long-lived Assets

The Company s long-lived assets primarily include property, plant and equipment, indefinite-lived assets, long-term investments and assets held for rent. The carrying values of long-lived assets are reviewed for impairment whenever events or changes in business circumstances indicate that the carrying amount of an asset may not be recoverable. An asset impairment is recognized when the carrying value of the asset is not recoverable based on the probability-weighted undiscounted estimated future cash flows to be generated by the asset. The Company s estimates reflect management s assumptions about selling prices, production and sales volumes, costs and market conditions over an estimate of the remaining operating period. If an impairment is indicated, the asset is written down to fair value. If the asset does not have a readily determinable market value, a discounted cash flow model may be used to determine the fair value of the asset. The key inputs to the discounted cash flow would be the same as the undiscounted cash flow noted above, with the addition of the discount rate used. In circumstances when an asset does not have separate identifiable cash flows, an impairment charge is recorded when the Company no longer intends to use the asset.

To test for impairment of assets the Company generally uses a probability-weighted estimate of the future undiscounted net cash flows of the assets over their remaining lives to determine if the value of the asset is recoverable. Long-lived assets are grouped with other assets and liabilities at the lowest level for which independent identifiable cash flows are determinable.

Income Tax in Interim Periods

The Company records its tax provision or benefit on an interim basis using an estimated annual effective tax rate. This rate is applied to the current period ordinary income or loss to determine the income tax provision or benefit allocated to the interim period. Losses from jurisdictions for which no benefit can be recognized and the income tax effects of unusual or infrequent items are excluded from the estimated annual effective tax rate and are recognized in the impacted interim period.

Valuation allowances are provided against the future tax benefits that arise from the deferred tax assets in jurisdictions for which no benefit can be recognized. The estimated annual effective tax rate may be significantly impacted by nondeductible expenses and the Company s projected earnings mix by tax jurisdiction. Adjustments to the estimated annual effective income tax rate are recognized in the period when such estimates are revised.

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

Inventory Valuation

Inventories are stated at the lower of cost or market. The cost of all carbon black inventories in the U.S. is determined using the last-in, first-out (LIFO) method. Had the Company used the first-in, first-out (FIFO) method instead of the LIFO method for such inventories, the value of those inventories would have been $40 million and $52 million higher as of March 31, 2015 and September 30, 2014, respectively. The cost of Specialty Fluids inventories is determined using the average cost method. The cost of other U.S. and non-U.S. inventories is determined using the FIFO method.

Cabot reviews inventory for both potential obsolescence and potential declines in anticipated selling prices. In this review, the Company makes assumptions about the future demand for and market value of the inventory, and based on these assumptions estimates the amount of any obsolete, unmarketable, slow moving or overvalued inventory. Cabot writes down the value of these inventories by an amount equal to the difference between the cost of the inventory and its estimated market value.

Pensions and Other Postretirement Benefits

The Company recognizes the funded status of defined benefit pension and other postretirement benefit plans as an asset or liability. This amount is defined as the difference between the fair value of plan assets and the benefit obligation. The Company is required to recognize as a component of other comprehensive income, net of tax, the actuarial gains/losses and prior service costs/credits that arise but were not previously required to be recognized as components of net periodic benefit cost. Other comprehensive income is adjusted as these amounts are later recognized in income as components of net periodic benefit cost.

Accumulated Other Comprehensive (Loss) Income

Accumulated other comprehensive (loss) income (AOCI), which is included as a component of stockholders equity, includes unrealized gains or losses on available-for-sale marketable securities, currency translation adjustments in foreign subsidiaries, translation adjustments on foreign equity securities and pension liability adjustments.

Recent Accounting Pronouncements

In July 2013, the Financial Accounting Standards Board (FASB) issued a new standard related to the Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists . The standard requires, unless certain conditions exist, an unrecognized tax benefit or a portion of an unrecognized tax benefit to be presented in the consolidated financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, similar to a tax loss or a tax credit carryforward. This standard is applicable for fiscal years beginning after December 15, 2013, and for interim periods within those years. The Company adopted this standard on October 1, 2014 and the implementation of the new standard did not have a material impact on its consolidated financial statements.

In April 2014, the FASB issued a new standard related to Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity . The standard requires discontinued operations treatment for disposals of a component or group of components of a business that represents a strategic shift that has or will have a major impact on an entity s operations or financial results and requires additional disclosures for discontinued operations and new disclosures for individually material disposal transactions that do not meet the definition of a discontinued operation. This standard is applicable for fiscal years beginning after December 15, 2014 and for interim periods within those years with early adoption permitted, but only for disposals that have not been reported in consolidated financial statements previously issued. The Company expects to adopt this standard beginning on October 1, 2015.

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

In May 2014, the FASB issued a new standard related to the Revenue from Contracts with Customers which amends the existing accounting standards for revenue recognition. The standard requires entities to recognize revenue when they transfer promised goods or services to customers in an amount that reflects the consideration the entity expects to be entitled to in exchange for those goods or services. This standard is applicable for fiscal years beginning after December 15, 2016 and for interim periods within those years and early adoption is not permitted. The Company expects to adopt this standard on October 1, 2017. In April 2015, the Financial Accounting Standards Board proposed deferring the effective date of the standard to annual periods beginning after December 15, 2017. The Company is currently evaluating the impact of the adoption of this standard on its consolidated financial statements.

In April 2015, the FASB issued a new standard simplifying the presentation of debt issuance costs by requiring debt issuance costs to be presented as a reduction of the corresponding debt liability. This will make the presentation of debt issuance costs consistent with the presentation of debt discounts or premiums. This standard is applicable for fiscal years beginning after December 15, 2015 and for interim periods within those years and early adoption is permitted. The Company expects to adopt this standard on October 1, 2016. The adoption of this standard is not expected to materially impact the Company s consolidated financial statements.

C. Acquisition of NHUMO

In November 2013, the Company purchased all of KUO s common stock in the NHUMO joint venture, which represented approximately 60% of the outstanding common stock of the joint venture. Prior to this transaction, the Company owned approximately 40% of the outstanding common stock of NHUMO, and the NHUMO entity was accounted for as an equity affiliate of the Company.

At the close of the transaction, the Company paid KUO $80 million in cash and NHUMO issued redeemable preferred stock to KUO with a redemption value of $25 million. The preferred stock accumulates dividends at a fixed rate of 6% annually and is redeemable at the option of KUO or the Company for $25 million starting in November 2018 or upon the occurrence of certain other conditions. Annual payment by NHUMO of the dividends is contingent on NHUMO achieving a minimum EBITDA (earnings before interest, taxes, depreciation and amortization) level and if such minimum EBITDA is not achieved in any year, the dividend will be accumulated and paid at the time the preferred shares are redeemed. The minimum EBITDA was achieved in 2014 and a dividend payment of $1.5 million was made in December 2014. The preferred stock issued in connection with the transaction is not mandatorily redeemable and has embedded put and call rights at the fixed redemption price. Accordingly, the instrument is accounted for as a financing obligation and has been separately presented in the Consolidated Balance Sheets as a long-term liability. Upon acquisition, the Company began consolidating NHUMO into its consolidated financial statements. Prior to closing, the Company received a $14 million dividend from NHUMO.

As of September 2014, the Company completed the valuation of its assets acquired and liabilities assumed. The allocation of the purchase price is based on the fair value of assets acquired and liabilities assumed, and Cabot s previously held equity interest in NHUMO as of the acquisition date. During fiscal 2014, the Company recorded certain measurement period adjustments which are presented in the table below. The measurement period adjustments and the related tax impact were immaterial to the Company s consolidated financial statements. The following table presents the components and allocation of the purchase price, including the measurement period adjustments:

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

	At Acquisition Date (October 31, 2013)	Measurement Period Adjustments	At Acquisition Date (As adjusted at September 30, 2014)
		(Dollars in millions)	
Assets			
Current assets	$ 54	$	$ 54
Property, plant and equipment	48		48
Other non-current assets	1		1
Intangible assets	57	6	63
Goodwill	51	(6)	45
Total assets acquired	211		211
Liabilities			
Accounts payable, accruals and other liabilities	(18)	(2)	(20)
Deferred tax liabilities - long-term	(31)	2	(29)
Total liabilities assumed	(49)		(49)
Net assets acquired	**$ 162**	**$**	**$ 162**
Cash consideration paid	80		
Fair value of redeemable preferred stock	28		
Previously held equity interest in NHUMO	54		
Total	**$ 162**		

As a result of the acquisition, the Company recorded a gain of $29 million for the difference between the carrying value and the fair value of the previously held equity interest in NHUMO, which was included in Other (expense) income in the first quarter of fiscal 2014. The fair value of $54 million for the previously held equity interest was determined based on the fair value of Cabot s pre-existing interest in NHUMO as adjusted for a control premium derived from synergies gained as a result of the Company obtaining control of NHUMO.

As part of the purchase price allocation, the Company determined that a separately identifiable intangible asset was customer relationships in the amount of $63 million, which is being amortized over a period of 20 years. The Company estimated the fair value of the identifiable acquisition-related intangible asset based on projections of cash flows that will arise from the asset. The projected cash flows are discounted to determine the fair value of the asset at the date of acquisition. The determination of the fair value of the intangible asset acquired required the use of significant judgment with regard to assumptions in the discounted cash flow model used.

The fair value of the redeemable preferred stock was determined based on a discounted cash flow model, using the expected timing of the cash flows and an appropriate discount rate.

The excess of the purchase price, which includes the cash consideration paid, the fair value of redeemable preferred stock and the previously held equity interest in NHUMO, over the fair value of the tangible net assets and intangible asset acquired, was recorded as goodwill. The goodwill recognized is attributable to the expected growth and operating synergies that the Company expects to realize from this acquisition. Goodwill generated from the acquisition is not deductible for tax purposes.

D. Discontinued Operations

In July 2014, the Company sold its Security Materials business to SICPA SA. The Consolidated Statements of Operations for all periods presented have been recast to reflect the Security Materials business in discontinued operations.

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

E. Employee Benefit Plans

Net periodic defined benefit pension and other postretirement benefit costs include the following:

	Three Months Ended March 31							
	2015		2014		2015		2014	
	Pension Benefits				Postretirement Benefits			
	U.S.	Foreign	U.S.	Foreign	U.S.	Foreign	U.S.	Foreign
	(Dollars in millions)							
Service cost	$	$ 3	$	$ 3	$	$	$	$
Interest cost	1	3	2	4	1			
Expected return on plan assets	(2)	(4)	(2)	(5)				
Amortization of prior service credit								
Amortization of actuarial loss		1		1				
Net periodic benefit (credit) cost	$ (1)	$ 3	$	$ 3	$ 1	$	$	$

	Six Months Ended March 31							
	2015		2014		2015		2014	
	Pension Benefits				Postretirement Benefits			
	U.S.	Foreign	U.S.	Foreign	U.S.	Foreign	U.S.	Foreign
	(Dollars in millions)							
Service cost	$	$ 5	$ 1	$ 5	$	$	$	$
Interest cost	3	6	4	8	1		1	
Expected return on plan assets	(5)	(8)	(5)	(10)				
Amortization of prior service credit					(1)		(1)	
Amortization of actuarial loss		2		2				
Settlement costs		18						
Net periodic benefit (credit) cost	$ (2)	$ 23	$	$ 5	$	$	$	$

Settlement of employee benefit plan

Effective October 1, 2014, the Company transferred the defined benefit obligations and pension plan assets in one of its foreign defined benefit plans to a multi-employer plan. This decision effectively moves the administrative, asset custodial, asset investment, actuarial, communication and benefit payment obligations to the multi-employer fund administrator. The plan is over 80% funded. Cabot is required to make contributions to the multi-employer fund and contributed assets by one participating employer may be used to provide benefits to employees of other participating employers since assets contributed by an employer are not segregated in a separate account or restricted to provide benefits only to employees of that employer. As a result of the transfer, a pre-tax charge of $18 million has been recorded in the six months ended March 31, 2015 as reflected in Settlement costs in the table above. The pre-tax charge consists of $27 million released from AOCI and $2 million of employer contributions at the time of the settlement, partially offset by an $11 million release of the pension liability. The settlement charge has been recorded primarily in Cost of sales in the Consolidated Statements of Operations.

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

F. Goodwill and Other Intangible Assets

Cabot had goodwill balances of $508 million and $536 million at March 31, 2015 and September 30, 2014, respectively. The carrying amount of goodwill attributable to each reportable segment with goodwill balances and the changes in those balances during the period ended March 31, 2015 are as follows:

	Reinforcement Materials	Performance Chemicals	Purification Solutions	Total
	(Dollars in millions)			
Balance at September 30, 2014	$ 68	$ 10	$ 458	$ 536
Foreign currency impact	(8)	(1)	(19)	(28)
Balance at March 31, 2015	$ 60	$ 9	$ 439	$ 508

Goodwill impairment tests are performed at least annually. The Company performed its last annual impairment assessment as of May 31, 2014 and determined there was no impairment. However, recent developments have occurred and continue to evolve that could impact the Purification Solutions reporting unit s fair value. Therefore, the Company currently believes that it is reasonably possible that an asset impairment charge may be required for the Purification Solutions reporting unit in the future, which could reduce the amount of goodwill attributable to the Purification Solutions reporting unit. Refer to the Intangible Assets and Goodwill disclosure included in Note B.

The following table provides information regarding the Company s intangible assets:

	March 31, 2015			September 30, 2014		
	Gross Carrying Value	Accumulated Amortization	Net Intangible Assets	Gross Carrying Value	Accumulated Amortization	Net Intangible Assets
	(Dollars in millions)					
Intangible assets with finite lives						
Developed technologies	$ 146	$ (19)	$ 127	$ 152	$ (16)	$ 136
Customer relationships	159	(20)	139	171	(17)	154
Total intangible assets, finite lives	$ 305	$ (39)	$ 266	$ 323	$ (33)	$ 290
Trademarks, indefinite lives	54		54	57		57

Total intangible assets	$ 359	$	(39)	$	320	$ 380	$	(33)	$	347

Intangible assets with finite lives are amortized over their estimated useful lives, which range from sixteen to twenty years, with a weighted average amortization period of approximately nineteen years. Amortization expense for the three months ended March 31, 2015 and 2014 was $4 million and $5 million, respectively, and is included in Cost of sales and Selling and administrative expenses in the Consolidated Statements of Operations. Amortization expense for the six months ended March 31, 2015 and 2014 was $8 million and $9 million, respectively, and is included in Cost of sales and Selling and administrative expenses in the Consolidated Statements of Operations. Total amortization expense is estimated to be approximately $16 million each year for the next five fiscal years. Intangible assets with indefinite lives are evaluated for impairment at least annually. The Company performed its annual impairment assessment as of May 31, 2014, and determined there was no impairment.

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

G. Stockholders Equity

In fiscal 2007, the Board of Directors authorized Cabot to repurchase up to ten million shares of Cabot s common stock in the open market or in privately negotiated transactions. This authorization did not have a set expiration date. During the first six months of fiscal 2015 and 2014, Cabot repurchased 925,700 and 379 shares, respectively, of its common stock under this authorization.

In January 2015, the Board of Directors authorized Cabot to repurchase up to five million shares of the Company s common stock in the open market or in privately negotiated transactions and cancelled the previous authorization. Cabot has repurchased 300,000 shares of its common stock under this authorization. As of March 31, 2015, 4.7 million shares remain available for repurchase under the current authorization.

During the first six months of fiscal 2015, Cabot paid cash dividends of $0.22 per share of common stock for a total of $28 million. During the first six months of fiscal 2014, Cabot paid cash dividends of $0.20 per share of common stock for a total of $26 million.

Noncontrolling interests

The following table illustrates the noncontrolling interests activity for the periods presented:

	2015	2014
	(Dollars in millions)	
Balance at September 30	$ 122	$ 132
Net income attributable to noncontrolling interests	5	9
Noncontrolling interest foreign currency translation adjustment	(3)	(2)
Noncontrolling interest dividends	(13)	(20)
Balance at March 31	$ 111	$ 119

H. Accumulated Other Comprehensive Loss

Comprehensive income combines net income and other comprehensive income items, which are reported as components of stockholders equity in the accompanying Consolidated Balance Sheets.

Changes in each component of AOCI, net of tax, are as follows:

	Currency Translation Adjustment	Unrealized Gains on Investments	Pension and Other Postretirement Benefit Liability Adjustments	Total
		(Dollars in millions)		
Balance at September 30, 2014, attributable to Cabot Corporation	$ 27	$ 2	$ (93)	$ (64)
Other comprehensive loss before reclassifications	(103)			(103)
Amounts reclassified from accumulated other comprehensive income			21	21
Net other comprehensive items	(103)		21	(82)
Less: Noncontrolling interest	(2)			(2)
Balance at December 31, 2014, attributable to Cabot Corporation	$ (74)	$ 2	$ (72)	$ (144)

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

	Currency Translation Adjustment	Unrealized Gains on Investments	Pension and Other Postretirement Benefit Liability Adjustments	Total
	(Dollars in millions)			
Balance at December 31, 2014, attributable to Cabot Corporation	$ (74)	$ 2	$ (72)	$ (144)
Other comprehensive loss before reclassifications	(131)			(131)
Amounts reclassified from accumulated other comprehensive income			1	1
Net other comprehensive items	(131)		1	(130)
Less: Noncontrolling interest	(1)			(1)
Balance at March 31, 2015, attributable to Cabot Corporation	$ (204)	$ 2	$ (71)	$ (273)

Accumulated other comprehensive items in the accompanying Consolidated Balance Sheets consist of the following items, net of tax:

	March 31, 2015	September 30, 2014
	(Dollars in millions)	
Foreign currency translation adjustments at beginning of period	$ 27	$ 154
Net foreign currency translation adjustments attributable to Cabot during the period	(231)	(127)
Balance at end of period	(204)	27
Unrealized gain on investments at beginning of period	2	2
Net unrealized gains during the period		
Balance at end of period	2	2

Pension and other postretirement benefit plans attributable to Cabot at beginning of period	(93)		(53)
Net change in pension and other postretirement benefit plans during the period	22		(40)
Balance at end of period	(71)		(93)
Total accumulated other comprehensive loss	$ (273)	$	(64)

18

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

The amounts reclassified out of AOCI and into the Statement of Operations for the three and six months ended March 31, 2015 and 2014 are as follows:

	Affected Line Item in the Consolidated Statements of Operations	Three Months Ended March 31, 2015	Three Months Ended March 31, 2014	Six Months Ended March 31, 2015	Six Months Ended March 31, 2014
		(Dollars in millions)			
Pension and other postretirement benefit liability adjustment					
Amortization of actuarial losses	Net Periodic Benefit Cost - see Note E for details	$ 1	$ 1	$ 2	$ 2
Amortization of prior service cost	Net Periodic Benefit Cost - see Note E for details			(1)	(1)
Settlement costs	Net Periodic Benefit Cost - see Note E for details			27	
Total before tax		1	1	28	1
Tax impact	Benefit for income taxes			(6)	
Total after tax		$ 1	$ 1	$ 22	$ 1

I. Commitments and Contingencies

Purchase Commitments

Cabot has entered into long-term purchase agreements primarily for the purchase of raw materials. Under certain of these agreements the quantity of material being purchased is fixed, but the price paid changes as market prices change. For those commitments, the amounts included in the table below are based on market prices at March 31, 2015.

Payments Due by Fiscal Year					
2016	2017	2018	2019	Thereafter	Total

	Remainder of Fiscal 2015						
	(Dollars in millions)						
Reinforcement Materials	$ 153	$ 239	$ 191	$ 191	$ 187	$ 2,099	$ 3,060
Performance Chemicals	34	57	34	30	29	210	394
Purification Solutions	10	9	7	7	7	8	48
Total	$ 197	$ 305	$ 232	$ 228	$ 223	$ 2,317	$ 3,502

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

Guarantee Agreements

Cabot has provided certain indemnities pursuant to which it may be required to make payments to an indemnified party in connection with certain transactions and agreements. In connection with certain acquisitions and divestitures, Cabot has provided routine indemnities with respect to such matters as environmental, tax, insurance, product and employee liabilities. In connection with various other agreements, including service and supply agreements with customers, Cabot has provided indemnities for certain contingencies and routine warranties. Cabot is unable to estimate the maximum potential liability for these types of indemnities as a maximum obligation is not explicitly stated in most cases and the amounts, if any, are dependent upon the outcome of future contingent events, the nature and likelihood of which cannot be reasonably estimated. The duration of the indemnities vary, and in many cases are indefinite. Cabot has not recorded any liability for these indemnities in the consolidated financial statements, except as otherwise disclosed.

Contingencies

Cabot is a defendant, or potentially responsible party, in various lawsuits and environmental proceedings wherein substantial amounts are claimed or at issue.

Environmental Matters

As of March 31, 2015 and September 30, 2014, Cabot had $17 million reserved for environmental matters, substantially all of which is accounted for on an undiscounted basis. These environmental matters mainly relate to closed sites. These reserves represent Cabot s best estimates of the probable costs to be incurred at those sites where costs are reasonably estimable based on the Company s analysis of the extent of clean up required, alternative clean-up methods available, abilities of other responsible parties to contribute and its interpretation of laws and regulations applicable to each site. Cash payments related to these environmental matters were less than $1 million and $1 million in the first six months of fiscal 2015 and 2014, respectively. Cabot reviews the adequacy of the reserves as circumstances change at individual sites and adjusts the reserves as appropriate. Almost all of Cabot s environmental issues relate to sites that are mature and have been investigated and studied and, in many cases, are subject to agreed upon remediation plans. However, depending on the results of future testing, changes in risk assessment practices, remediation techniques and regulatory requirements, newly discovered conditions, and other factors, it is reasonably possible that the Company could incur additional costs in excess of environmental reserves currently recorded. Management estimates, based on the latest available information, that any such future environmental remediation costs that are reasonably possible to be in excess of amounts already recorded would be immaterial to the Company s consolidated financial statements.

Other Matters

Respirator Liabilities

Cabot has exposure in connection with a safety respiratory products business that a subsidiary acquired from American Optical Corporation (AO) in an April 1990 asset purchase transaction. The subsidiary manufactured respirators under the AO brand and disposed of that business in July 1995. In connection with its acquisition of the business, the Cabot subsidiary agreed, in certain circumstances, to assume a portion of AO s liabilities, including costs of legal fees together with amounts paid in settlements and judgments, allocable to AO respiratory products used prior to the 1990 purchase by the Cabot subsidiary. In exchange for the subsidiary s assumption of certain of AO s respirator liabilities, AO agreed to provide to the subsidiary the benefits of: (i) AO s insurance coverage for the period prior to the 1990 acquisition and (ii) a former owner s indemnity of AO holding it harmless from any liability allocable to AO respiratory products used prior to May 1982. As more fully described in the 2014 10-K, the respirator liabilities generally involve claims for personal injury, including asbestosis, silicosis and coal worker s pneumoconiosis, allegedly resulting from the use of respirators that are alleged to have been negligently designed and/or labeled.

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

As of March 31, 2015 and September 30, 2014, there were approximately 40,000 and 41,000 claimants, respectively, in pending cases asserting claims against AO in connection with respiratory products. Cabot has a reserve to cover its expected share of liability for existing and future respirator liability claims. At March 31, 2015 and September 30, 2014, the reserve was $11 million and $13 million, respectively. Cash payments related to this liability were $2 million in the first six months of both fiscal 2015 and 2014.

Other

The Company is subject to various other lawsuits, claims and contingent liabilities arising in the ordinary course of its business and with respect to the Company s divested businesses. In the opinion of the Company, although final disposition of some or all of these other suits and claims may impact the Company s consolidated financial statements in a particular period, they are not expected, in the aggregate, to have a material adverse effect on the Company s financial position.

J. Income Tax Uncertainties

Cabot files U.S. federal and state and non-U.S. income tax returns in jurisdictions with varying statutes of limitations. The 2011 through 2014 tax years remain subject to examination by the United States Internal Revenue Service (IRS) and various tax years from 2005 through 2014 remain subject to examination by the respective state tax authorities. In significant non-U.S. jurisdictions, various tax years from 2004 through 2014 remain subject to examination by their respective tax authorities. Cabot s significant non-U.S. jurisdictions include China, France, Germany, Italy, Japan, and the Netherlands.

Certain Cabot subsidiaries are under audit in jurisdictions outside of the U.S. In addition, certain statutes of limitations are scheduled to expire in the near future. It is reasonably possible that a change in the unrecognized tax benefits may also occur within the next twelve months related to the settlement of one or more of these audits, however, an estimated range of the impact on the unrecognized tax benefits cannot be quantified at this time.

During the three and six months ended March 31, 2015, Cabot released uncertain tax positions of $1 million and $12 million, respectively, due to the expirations of statutes of limitations in various jurisdictions. As of October 1, 2014, Cabot adopted a new accounting standard which requires, unless certain conditions exist, an unrecognized tax benefit or a portion of an unrecognized tax benefit be presented in the consolidated financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, similar to a tax loss or a tax credit carryforward. This resulted in a reduction of the liability for uncertain tax positions and deferred tax assets of $5 million.

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

K. Earnings Per Share

The following tables summarize the components of the basic and diluted earnings per common share computations:

	Three Months Ended March 31		Six Months Ended March 31	
	2015	2014	2015	2014
	(Dollars and shares in millions, except per share amounts)			
Basic EPS:				
Net income attributable to Cabot Corporation	$ 26	$ 36	$ 71	$ 116
Less: Dividends and dividend equivalents to participating securities				
Less: Undistributed earnings allocated to participating securities[(1)]				1
Earnings allocated to common shareholders (numerator)	$ 26	$ 36	$ 71	$ 115
Weighted average common shares and participating securities outstanding	64.1	65.0	64.4	64.8
Less: Participating securities[(1)]	0.5	0.6	0.5	0.6
Adjusted weighted average common shares (denominator)	63.6	64.4	63.9	64.2
Amounts per share - basic:				
Income from continuing operations attributable to Cabot Corporation	$ 0.41	$ 0.56	$ 1.11	$ 1.81
Loss from discontinued operations		(0.01)		(0.02)
Net income attributable to Cabot Corporation	$ 0.41	$ 0.55	$ 1.11	$ 1.79
Diluted EPS:				
Earnings allocated to common shareholders	$ 26	$ 36	$ 71	$ 115
Plus: Earnings allocated to participating securities				1

Less: Adjusted earnings allocated to participating securities[2]				(1)
Earnings allocated to common shareholders (numerator)	$ 26	$ 36	$ 71	$ 115
Adjusted weighted average common shares outstanding	63.6	64.4	63.9	64.2
Effect of dilutive securities:				
Common shares issuable[3]	0.5	0.7	0.5	0.8
Adjusted weighted average common shares (denominator)	64.1	65.1	64.4	65.0
Amounts per share - diluted:				
Income from continuing operations attributable to Cabot Corporation	$ 0.41	$ 0.55	$ 1.10	$ 1.79
Loss from discontinued operations		(0.01)		(0.02)
Net income attributable to Cabot Corporation	$ 0.41	$ 0.54	$ 1.10	$ 1.77

(1) Participating securities consist of shares of unvested restricted stock and unvested time-based restricted stock units.

22

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

Undistributed earnings are the earnings which remain after dividends declared during the period are assumed to be distributed to the common and participating shareholders. Undistributed earnings are allocated to common and participating shareholders on the same basis as dividend distributions. The calculation of undistributed earnings is as follows:

	Three Months Ended March 31		Six Months Ended March 31	
	2015	2014	2015	2014
	(Dollars in millions)			
Calculation of undistributed earnings:				
Net income attributable to Cabot Corporation	$ 26	$ 36	$ 71	$ 116
Less: Dividends declared on common stock	14	13	28	26
Less: Dividends declared on participating securities				
Undistributed earnings	$ 12	$ 23	$ 43	$ 90
Allocation of undistributed earnings:				
Undistributed earnings allocated to common shareholders	$ 12	$ 23	$ 43	$ 89
Undistributed earnings allocated to participating shareholders				1
Undistributed earnings	$ 12	$ 23	$ 43	$ 90

(2) Undistributed earnings are adjusted for the assumed distribution of dividends to the dilutive securities, which are described in (3) below, and then reallocated to participating securities.

(3) Represents incremental shares of common stock from the (i) assumed exercise of stock options issued under Cabot s equity incentive plans; (ii) assumed issuance of shares to employees pursuant to the Company s Deferred Compensation and Supplemental Retirement Plan; and (iii) assumed issuance of shares under outstanding performance-based restricted stock unit awards issued under Cabot s equity incentive plans. For the three and six months ended March 31, 2015, 437,647 and 380,981 incremental shares of common stock, respectively, were not included in the calculation of diluted earnings per share because the inclusion of these shares would have been antidilutive. For the three and six months ended March 31, 2014, 203,019 and 220,866 incremental shares of common stock, respectively, were not included in the calculation of diluted earnings per share because the

inclusion of these shares would have been antidilutive.

L. Restructuring

Cabot s restructuring activities were recorded in the Consolidated Statements of Operations as follows:

	Three Months Ended March 31		Six Months Ended March 31	
	2015	2014	2015	2014
	(Dollars in millions)			
Cost of sales	$ 1	$ 5	$ 3	$ 9
Selling and administrative expenses	4	11	9	12
Total	$ 5	$ 16	$ 12	$ 21

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

Details of these restructuring activities and the related reserves during the three months ended March 31, 2015 are as follows:

	Severance and Employee Benefits	Environmental Remediation	Other	Total
	(Dollars in millions)			
Reserve at December 31, 2014	$ 14	$ 2	$ 1	$ 17
Charges	2	1	2	5
Cash paid	(6)		(2)	(8)
Foreign currency translation adjustment	(1)			(1)
Reserve at March 31, 2015	$ 9	$ 3	$ 1	$ 13

Details of these restructuring activities and the related reserves during the six months ended March 31, 2015 are as follows:

	Severance and Employee Benefits	Environmental Remediation	Asset Impairment and Accelerated Depreciation	Other	Total
	(Dollars in millions)				
Reserve at September 30, 2014	$ 16	$ 2	$	$ 1	$ 19
Charges	5	1	1	5	12
Costs charged against assets / liabilities			(1)		(1)
Cash paid	(10)			(5)	(15)
Foreign currency translation adjustment	(2)				(2)
Reserve at March 31, 2015	$ 9	$ 3	$	$ 1	$ 13

Business Service Center Transition

In January 2014, the Company announced its intention to open a new Europe, Middle East and Africa (EMEA) business service center in Riga, Latvia, and to close its Leuven, Belgium site, subject to the Belgian information and consultation process, which was completed in June 2014. These actions were developed following an extensive evaluation of the Company s business service capabilities in the EMEA region and a determination that the future EMEA business service center will enable the Company to provide the highest quality of service at the most competitive cost.

The Company expects that the majority of actions related to the transition of the business service center will be completed by the end of fiscal 2015 and result in total charges of approximately $24 million, comprised of $16 million of severance charges and $8 million of other transition costs. Through March 31, 2015, the Company has recorded $23 million for this plan comprised of $16 million severance charges and $7 million of other transition costs

The Company has recorded $5 million and $14 million of charges in the first six months of fiscal 2015 and 2014, respectively related to this plan. Fiscal 2014 costs were comprised primarily of employee severance costs whereas fiscal 2015 costs include severance charges of $1 million and $4 million of other transition costs including training costs and redundant salaries. The Company has recorded $1 million and $14 million of charges in the three months ended March 31, 2015 and 2014, respectively, related to this plan, comprised of severance and other transition costs.

Cumulative cash outlays related to this plan are expected to be approximately $22 million, comprised of $14 million of severance payments and $8 million of transition costs. Through March 31, 2015, the Company has made $16 million in cash payments related to this plan, comprised of $7 million of transition costs and $9 million of severance costs, and expects to make additional cash payments of approximately $6 million during the remainder of fiscal 2015 and thereafter, comprised of $5 million of severance costs and $1 million of other transition costs.

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

As of March 31, 2015, Cabot has $5 million of accrued restructuring costs in the Consolidated Balance Sheet related to this closure comprised of accrued severance charges.

Closure of Port Dickson, Malaysia Manufacturing Facility

On April 26, 2013, the Company announced that the Board of its carbon black joint venture, Cabot Malaysia Sdn. Bhd. (CMSB), decided to cease production at its Port Dickson, Malaysia facility. The facility ceased production in June 2013. The Company holds a 50.1 percent equity share in CMSB. The decision, which affected approximately 90 carbon black employees, was driven by the facility s manufacturing inefficiencies and raw materials costs.

Through March 31, 2015, the Company recorded pre-tax restructuring charges related to this plan of $20 million comprised mainly of accelerated depreciation and asset write-offs of $15 million, severance charges of $2 million, site demolition, clearing and environmental remediation charges of $2 million, and other closure related charges of $1 million. CMSB s net income or loss is attributable to Cabot Corporation and to the noncontrolling interest in the joint venture. The Company has recorded pre-tax charges of less than $1 million and $2 million in the six months ended March 31, 2015 and 2014, respectively, related to this closure and less than $1 million and $1 million for the three months ended March 31, 2015 and 2014, respectively. The portion of the charges that are allocable to the noncontrolling interest in CMSB (49.9%) are recorded within Net income attributable to noncontrolling interests, net of tax, in the Consolidated Statements of Operations. The majority of actions related to closure of the plant were completed in fiscal 2014.

Cumulative net cash outlays related to this plan are expected to be approximately $5 million comprised primarily of $2 million for site demolition, clearing and environmental remediation, $2 million for severance, and $1 million for other closure related charges. Through March 31, 2015, CMSB has made approximately $3 million in cash payments related to this plan mainly for severance and site demolition and clearing costs.

CMSB expects to make net cash payments of $2 million during the remainder of fiscal 2015 and thereafter mainly for site demolition, clearing and environmental remediation costs. These amounts exclude any proceeds that may be received from the sale of land or other manufacturing assets.

As of March 31, 2015, Cabot has $1 million of accrued restructuring costs in the Consolidated Balance Sheets related to this closure, which is mainly for accrued environmental and other charges.

Other Activities

The Company has recorded pre-tax charges of approximately $4 million during both the first six months of fiscal 2015 and 2014, and $3 million and less than $1 million for the three months ended March 31, 2015 and 2014, respectively, related to restructuring activities at several other locations. Fiscal 2015 charges are comprised of severance costs whereas fiscal 2014 charges are comprised of accelerated depreciation and asset write-offs. The Company anticipates that it will record additional charges of $1 million in the remainder of fiscal 2015 related to these actions.

The Company made payments of $2 million related to these actions in the first six months of fiscal 2015 and expects to pay $5 million in the remainder of fiscal 2015 and thereafter mainly for severance and other closure related costs at the impacted locations.

As of March 31, 2015, Cabot has $4 million of accrued severance and other closure related costs in the Consolidated Balance Sheets related to these activities.

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

Previous Actions and Sites Pending Sale

Beginning in fiscal 2009, the Company entered into several different restructuring plans which have been substantially completed, pending the sale of former manufacturing sites in Thane, India and Hong Kong. The Company has incurred total cumulative pre-tax charges of approximately $165 million related to these plans through March 31, 2015, comprised of $67 million for severance charges, $66 million for accelerated depreciation and asset impairments, $10 million for environmental, demolition and site clearing costs, and $23 million of other closure related charges, partially offset by gains on asset sales of $1 million. These amounts do not include any gain that may be recorded if the Company successfully sells its land rights and certain manufacturing related assets in India and Hong Kong.

Pre-tax restructuring expenses related to these plans were approximately $2 million and $1 million during the first six months of fiscal 2015 and 2014, respectively, and less than $1 million and $1 million in the three months ended March 31, 2015 and 2014, respectively. Since fiscal 2009, Cabot has made net cash payments of $86 million related to these plans and expects to pay approximately $3 million in the remainder of fiscal 2015 and thereafter. The remaining payments consist mainly of environmental and other closure related costs.

As of March 31, 2015, Cabot has $3 million of accrued environmental, severance and other closure related costs in the Consolidated Balance Sheets related to these activities.

M. Financial Instruments and Fair Value Measurements

The FASB authoritative guidance on fair value measurements defines fair value, provides a framework for measuring fair value in generally accepted accounting principles, and requires certain disclosures about fair value measurements. The disclosures focus on the inputs used to measure fair value. The guidance establishes the following hierarchy for categorizing these inputs:

Level 1	Quoted market prices in active markets for identical assets or liabilities
Level 2	Significant other observable inputs (e.g., quoted prices for similar items in active markets, quoted prices for identical or similar items in markets that are not active, inputs other than quoted prices that are observable such as interest rate and yield curves, and market-corroborated inputs)
Level 3	Significant unobservable inputs

There were no transfers of financial assets or liabilities measured at fair value between Level 1 and Level 2, or transfers into or out of Level 3, during the first six months of both fiscal 2015 and 2014.

At March 31, 2015 and September 30, 2014, the fair value of guaranteed investment contracts, included in Other assets in the Consolidated Balance Sheets, was $11 million and $13 million, respectively which approximated carrying values in both periods Guaranteed investment contracts were classified as Level 2 instruments within the fair value hierarchy as the fair value determination was based on other observable inputs.

At March 31, 2015 and September 30, 2014, the fair values of cash and cash equivalents, accounts and notes receivable, accounts payable and accrued liabilities, and notes payable and variable rate debt approximated their carrying values due to the short-term nature of these instruments. The carrying values and fair values of the long-term fixed rate debt were $0.98 billion and $1.05 billion, respectively, as of both March 31, 2015 and September 30, 2014. The fair values of Cabot s fixed rate long-term debt and capital lease obligations are estimated based on comparable quoted market prices at the respective period ends. The carrying amounts of Cabot s floating rate long-term debt and capital lease obligations approximate their fair values. All such measurements are based on observable inputs and are classified as Level 2 within the fair value hierarchy. The valuation technique used is the discounted cash flow model.

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

N. Derivatives

Interest Rate Risk Management

Cabot s objective is to maintain a certain fixed-to-variable interest rate mix on the Company s debt obligations. Cabot may enter into interest rate swaps as a hedge of the underlying debt instruments to effectively change the characteristics of the interest rate without changing the debt instrument. As of both March 31, 2015 and September 30, 2014, there were no derivatives held to manage interest risk.

Foreign Currency Risk Management

Cabot s international operations are subject to certain risks, including currency exchange rate fluctuations and government actions. Cabot endeavors to match the currency in which debt is issued to the currency of the Company s major, stable cash receipts. In some situations Cabot has issued debt denominated in U.S. dollars and then entered into cross currency swaps that exchange the dollar principal and interest payments into a currency where the Company expects long-term, stable cash receipts.

Additionally, the Company has foreign currency exposure arising from its net investments in foreign operations. Cabot, from time to time, enters into cross-currency swaps to mitigate the impact of currency rate changes on the Company s net investments.

The Company also has foreign currency exposure arising from the denomination of monetary assets and liabilities in foreign currencies other than the functional currency of a given subsidiary as well as the risk that currency fluctuations could affect the dollar value of future cash flows generated in foreign currencies. Accordingly, Cabot uses short-term forward contracts to minimize the exposure to foreign currency risk. In certain situations where the Company has forecasted purchases under a long-term commitment or forecasted sales denominated in a foreign currency, Cabot may enter into appropriate financial instruments in accordance with the Company s risk management policy to hedge future cash flow exposures.

The following table provides details of the derivatives held as of March 31, 2015 and September 30, 2014 to manage foreign currency risk.

		Notional Amount, net		
Description	**Borrowing**	**March 31, 2015**	**September 30, 2014**	**Hedge Designation**
Forward Foreign Currency Contracts [(1)]	N/A	USD 8 million	USD 32 million	No designation

(1) Cabot s forward foreign exchange contracts are denominated primarily in the Brazilian real, British pound sterling, Colombian peso, Czech koruna, and Indonesian rupiah.

Accounting for Derivative Instruments and Hedging Activities

The Company determines the fair value of financial instruments using quoted market prices whenever available. When quoted market prices are not available for various types of financial instruments (such as forwards, options and swaps), the Company uses standard models with market-based inputs, which take into account the present value of estimated future cash flows and the ability of the financial counterparty to perform. For interest rate and cross-currency swaps, the significant inputs to these models are interest rate curves for discounting future cash flows. For forward foreign currency contracts, the significant inputs are interest rate curves for discounting future cash flows, and exchange rate curves of the foreign currency for translating future cash flows.

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

Fair Value Hedge

For derivative instruments that are designated and qualify as fair value hedges, the gain or loss on the derivative as well as the offsetting gain or loss on the hedged item attributable to the hedged risk are recognized in current period earnings.

Cash Flow Hedge

For derivative instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative is recorded in AOCI and reclassified to earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current period earnings.

Other Derivative Instruments

From time to time, the Company may enter into certain derivative instruments that may not be designated as hedges for accounting purposes, which include cross currency swaps, foreign currency forward contracts and commodity derivatives. For cross currency swaps and foreign currency forward contracts not designated as hedges, the Company uses standard models with market-based inputs. The significant inputs to these models are interest rate curves for discounting future cash flows, and exchange rate curves of the foreign currency for translating future cash flows. In determining the fair value of the commodity derivatives, the significant inputs to valuation models are quoted market prices of similar instruments in active markets. Although these derivatives do not qualify for hedge accounting, Cabot believes that such instruments are closely correlated with the underlying exposure, thus managing the associated risk. The gains or losses from changes in the fair value of derivative instruments that are not accounted for as hedges are recognized in current period earnings.

For both March 31, 2015 and September 30, 2014, the fair value of derivative instruments were immaterial and were presented in Prepaid expenses and other current assets and Accounts payable and accrued liabilities on the Consolidated Balance Sheets.

The net after-tax amounts to be reclassified from AOCI to earnings within the next 12 months are expected to be immaterial.

O. Venezuela

Cabot owns 49% of an operating carbon black affiliate in Venezuela, which is accounted for as an equity affiliate, through wholly-owned subsidiaries that carry the investment and receive its dividends. As of March 31, 2015, these subsidiaries carried the operating affiliate investment of $15 million and held 19 million bolivars (less than $1 million) in cash.

During each of the six months ended March 31, 2015 and 2014, the operating affiliate declared a dividend in the amount of $4 million which were paid in U.S. dollars and repatriated to the Company s wholly-owned subsidiaries.

A significant portion of the Company s operating affiliate s sales are exports denominated in U.S. dollars. The Venezuelan government mandates that a certain percentage of the dollars collected from these sales be converted into bolivars. The operating affiliate and the Company s wholly owned subsidiaries used an exchange rate that is available to the Company when converting these dollars into bolivars to remeasure their bolivar denominated monetary accounts. The exchange rate made available to the Company on March 31, 2015 was 52 bolivars to the U.S. dollar (B/$).

The operating entity has generally been profitable. The Company continues to closely monitor developments in Venezuela and their potential impact on the recoverability of its equity affiliate investment.

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

The Company closely monitors its ability to convert its bolivar holdings into U.S. dollars, as the Company intends to convert substantially all bolivars held by its wholly-owned subsidiaries in Venezuela to U.S. dollars as soon as practical. Any future change in the exchange rate made available to the Company or opening of additional parallel markets could cause the Company to change the exchange rate it uses and result in gains or losses on the bolivar denominated assets held by its operating affiliate and wholly-owned subsidiaries.

P. Financial Information by Segment

The Company identifies a business as an operating segment if: i) it engages in business activities from which it may earn revenues and incur expenses; ii) its operating results are regularly reviewed by the Chief Operating Decision Maker (CODM) to make decisions about resources to be allocated to the segment and assess its performance; and iii) it has available discrete financial information. The Company has determined that all of its reported businesses are operating segments. The CODM reviews financial information at the operating segment level to allocate resources and to assess the operating results and financial performance for each operating segment. Operating segments are aggregated if the operating segments are determined to have similar economic characteristics and if the operating segments are similar in the following areas: i) nature of products and services; ii) nature of production processes; iii) type or class of customer for their products and services; iv) methods used to distribute the products or provide services; and v) if applicable, the nature of the regulatory environment.

In December 2014, the Company realigned its business reporting structure into four segments that consist of Reinforcement Materials, Performance Chemicals, Purification Solutions and Specialty Fluids. Segment results have been recast for all periods presented to reflect the realignment of the Company s global business segments. The new segment structure is designed to improve efficiency and resource prioritization and reflects how the Company s CODM reviews segment results to assess performance and allocate resources.

The Reinforcement Materials segment combines the rubber blacks and elastomer composites product lines.

The Performance Chemicals segment combines the specialty carbons and compounds and inkjet colorants product lines into the Specialty Carbons and Formulations business, and combines the fumed metal oxides and aerogel product lines into the Metal Oxides business. These businesses are similar in terms of economic characteristics, nature of products, processes, customer class and product distribution methods, and therefore have been aggregated into one reportable segment.

The Purification Solutions segment represents the Company s activated carbon business and the Specialty Fluids segment includes cesium formate oil and gas drilling fluids and high-purity fine cesium chemicals.

Reportable segment operating profit (loss) before interest and taxes (Segment EBIT) is presented for each reportable segment in the financial information by reportable segment table below on the line entitled Income (loss) from continuing operations before taxes. Segment EBIT excludes certain items, meaning items management does not consider representative of segment results. In addition, Segment EBIT includes Equity in earnings (loss) of affiliated companies, net of tax, the full operating results of a contractual joint venture in Purification Solutions, royalties, Net income attributable to noncontrolling interests, net of tax, and discounting charges for certain Notes receivable, but excludes Interest expense, foreign currency transaction gains and losses, interest income, dividend income, unearned revenue, the effects of LIFO accounting for inventory, general unallocated expense and unallocated corporate costs.

Table of Contents

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

Financial information by reportable segment is as follows:

	Reinforcement Materials	Performance Chemicals	Purification Solutions	Specialty Fluids	Segment Total	Unallocated and Other[1]	Consolidated Total
				(Dollars in millions)			
Three Months Ended March 31, 2015							
Revenues from external customers[2]	$ 358	$ 237	$ 71	$ 8	$ 674	$ 20	$ 694
Income (loss) from continuing operations before taxes[3]	$ 27	$ 42	$ 1	$ (1)	$ 69	$ (30)	$ 39
Three Months Ended March 31, 2014							
Revenues from external customers[2]	$ 512	$ 264	$ 80	$ 25	$ 881	$ 17	$ 898
Income (loss) from continuing operations before taxes[3]	$ 65	$ 46	$ (4)	$ 9	$ 116	$ (68)	$ 48
Six Months Ended March 31, 2015							
Revenues from external customers[2]	$ 818	$ 466	$ 147	$ 24	$ 1,455	$ 51	$ 1,506
Income (loss) from continuing operations before taxes[3]	$ 80	$ 81	$	$ 5	$ 166	$ (76)	$ 90
Six Months Ended March 31, 2014							
Revenues from external customers[2]	$ 1,045	$ 501	$ 152	$ 53	$ 1,751	$ 45	$ 1,796
Income (loss) from continuing operations before taxes[3]	$ 138	$ 83	$ (13)	$ 22	$ 230	$ (73)	$ 157

(1)

Unallocated and Other includes certain items and eliminations necessary to reflect management s reporting of operating segment results. These items are reflective of the segment reporting presented to the Chief Operating Decision Maker.

(2) Unallocated and Other reflects royalties, other operating revenues, external shipping and handling costs, the impact of unearned revenue, the removal of 100% of the sales of an equity method affiliate and discounting charges for certain Notes receivable. Details are provided in the table below:

	Three Months Ended March 31		Six Months Ended March 31	
	2015	**2014**	**2015**	**2014**
	(Dollars in millions)			
Royalties, other operating revenues, the impact of unearned revenue, the removal of 100% of the sales of an equity method affiliate and discounting charges for certain Notes receivable.	$ (8)	$ (12)	$ (4)	$ (12)
Shipping and handling fees	28	29	55	57
Total	$ 20	$ 17	$ 51	$ 45

30

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

(3) Income (loss) from continuing operations before taxes that are categorized as Unallocated and Other includes:

	Three Months Ended March 31		Six Months Ended March 31	
	2015	2014	2015	2014
	(Dollars in millions)			
Interest expense	$ (14)	$ (13)	$ (27)	$ (27)
Total certain items, pre-tax[a]	(6)	(36)	(32)	(12)
Equity in (earnings) loss of affiliated companies, net of tax[b]	(2)	2	(3)	
Unallocated corporate costs[c]	(11)	(16)	(23)	(29)
General unallocated income (expense)[d]	3	(5)	9	(5)
Total	$ (30)	$ (68)	$ (76)	$ (73)

(a) Certain items are items that management does not consider to be representative of operating segment results and they are, therefore, excluded from Segment EBIT. Certain items, pre-tax, for the three months ended March 31, 2015 include $5 million related to global restructuring activities and $1 million for acquisition and integration-related charges. Certain items, pre-tax, for the six months ended March 31, 2015 include $12 million related to global restructuring activities, $2 million for acquisition and integration-related charges and $18 million related to an employee benefit plan settlement charge. Certain items, pre-tax, for the three months ended March 31, 2014 include $16 million related to global restructuring activities, $6 million of foreign currency loss on revaluations and $14 million for legal and environmental matters and reserves. Certain items, pre-tax, for the six months ended March 31, 2014 include $21 million related to global restructuring activities, $5 million for acquisition and integration-related charges (consisting of $3 million for certain other one-time integration costs and $2 million of additional charges related to acquisition accounting adjustments for the acquired inventory of NHUMO) and $15 million for legal and environmental matters and reserves offset by a $29 million non-cash gain recognized on the Company s pre-existing investment in NHUMO as a result of the NHUMO transaction.

(b) Equity in (earnings) loss of affiliated companies, net of tax is included in Segment EBIT and is removed from Unallocated and other to reconcile to income (loss) from operations before taxes.

(c) Unallocated corporate costs are not controlled by the segments and primarily benefit corporate interests.

(d) General unallocated income consists of gains (losses) arising from foreign currency transactions, net of other foreign currency risk management activities, the impact of accounting for certain inventory on a LIFO basis, the profit or loss related to the corporate adjustment for unearned revenue, and the impact of including the full operating results of an equity affiliate in Purification Solutions Segment EBIT.

Performance Chemicals is comprised of two businesses that sell the following products: specialty grades of carbon black, thermoplastic concentrates and compounds and inkjet colorants (the Specialty Carbons and Formulation business); and fumed silica, fumed alumina and dispersions thereof, and aerogel (the Metal Oxides business). The net sales from each of these businesses for the three and six months ended March 31, 2015 and 2014 are as follows:

	Three Months Ended March 31		**Six Months Ended March 31**	
	2015	**2014**	**2015**	**2014**
	(Dollars in millions)			
Specialty Carbons and Formulations	$ 162	$ 186	$ 319	$ 349
Metal Oxides	75	78	147	152
Total Performance Chemicals	$ 237	$ 264	$ 466	$ 501

31

Table of Contents

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations
Critical Accounting Policies

The preparation of our consolidated financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues, and expenses and related disclosure of contingent assets and liabilities. We consider an accounting estimate to be critical to the consolidated financial statements if (i) the estimate is complex in nature or requires a high degree of judgment and (ii) different estimates and assumptions were used, the results could have a material impact on the consolidated financial statements. On an ongoing basis, we evaluate our policies and estimates. We base our estimates on historical experience, current conditions and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. The estimates that we believe are critical to the preparation of the consolidated financial statements are presented below.

Revenue Recognition and Accounts Receivable

We recognize revenue when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price is fixed or determinable and collectability is reasonably assured. We generally are able to ensure that products meet customer specifications prior to shipment. If we are unable to determine that the product has met the specified objective criteria prior to shipment or if title has not transferred because of sales terms, the revenue is considered unearned and is deferred until the revenue recognition criteria are met. Shipping and handling charges related to sales transactions are recorded as sales revenue when billed to customers or included in the sales price.

The following table shows the relative size of the revenue recognized in each of our reportable segments for the periods presented.

	Three Months Ended March 31		Six Months Ended March 31	
	2015	**2014**	**2015**	**2014**
Reinforcement Materials	53%	58%	56%	59%
Performance Chemicals	35%	30%	32%	29%
Purification Solutions	11%	9%	10%	9%
Specialty Fluids	1%	3%	2%	3%

We derive the substantial majority of revenues from the sale of products in Reinforcement Materials and Performance Chemicals. Revenue from these products is typically recognized when the product is shipped and title and risk of loss have passed to the customer. Depending on the nature of the contract with the customer, a portion of the segment s revenue may be recognized using proportional performance. We have technology and licensing agreements with one customer that are accounted for as multiple element arrangements. Revenue is recognized ratably over the term of the agreements, limited by the cumulative amounts that become due, some of which are through 2022. We offer certain customers cash discounts and volume rebates as sales incentives. The discounts and volume rebates are recorded as a reduction in sales at the time revenue is recognized and are estimated based on historical experience and contractual obligations. We periodically review the assumptions underlying estimates of discounts and volume rebates and adjust revenues accordingly.

Revenue in Purification Solutions is typically recognized when the product is shipped and title and risk of loss have passed to the customer. For major activated carbon injection systems projects, revenue is recognized using the percentage-of-completion method.

A significant portion of the revenue in Specialty Fluids arises primarily from the rental of cesium formate. This revenue is recognized throughout the rental period based on the contracted rental terms. Customers are also billed and revenue is recognized, typically at the end of the job, for cesium formate product that is not returned. We also generate revenues from cesium formate sold outside of a rental process and revenue is recognized upon delivery of the fluid.

We maintain allowances for doubtful accounts based on an assessment of the collectability of specific customer accounts, the aging of accounts receivable and other economic information on both an historical and prospective basis. Customer account balances are charged against the allowance when it is probable the receivable will not be recovered. There is no material off-balance sheet credit exposure related to customer receivable balances.

Intangible Assets and Goodwill

We record tangible and intangible assets acquired and liabilities assumed in business combinations under the acquisition method of accounting. Amounts paid for an acquisition are allocated to the assets acquired and liabilities assumed based on their fair values at the date of acquisition. Goodwill is comprised of the purchase price of business acquisitions in excess of the fair value assigned to the net tangible and identifiable intangible assets acquired. Goodwill is not amortized, but is reviewed for impairment annually as of May 31, or when events or changes in the business environment indicate that the carrying value of the reporting unit may exceed its fair value. A reporting unit, for the purpose of the impairment test, is at or below the operating segment level, and constitutes a business for which discrete financial information is available and regularly reviewed by segment management. The separate businesses included within Performance Chemicals are considered separate reporting units. The goodwill balance relative to this segment is recorded in the Metal Oxides reporting unit within Performance Chemicals.

For the purpose of the goodwill impairment test, we first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If an initial qualitative assessment identifies that it is more likely than not that the carrying value of a reporting unit exceeds its estimated fair value, an additional quantitative evaluation is performed under the two-step impairment test. Alternatively, we may elect to proceed directly to the quantitative goodwill impairment test. If based on the quantitative evaluation the fair value of the reporting unit is less than its carrying amount, we perform an analysis of the fair value of all assets and liabilities of the reporting unit. If the implied fair value of the reporting unit s goodwill is determined to be less than its carrying amount, an impairment is recognized for the difference. The fair value of a reporting unit is based on discounted estimated future cash flows. The fair value is also benchmarked against a market approach using the guideline public companies method. The assumptions used to estimate fair value include management s best estimates of future growth rates, operating cash flows, capital expenditures and discount rates over an estimate of the remaining operating period at the reporting unit level. Should the fair value of any of our reporting units decline because of reduced operating performance, market declines, changes in the discount rate, or other indicators of impairment, charges for impairment may be necessary. Based on our most recent annual goodwill impairment test performed as of May 31, 2014, the fair values of the Reinforcement Materials and Metal Oxides reporting units were substantially in excess of their carrying values. At that date, the fair value of the Purification Solutions reporting unit exceeded its carrying value by approximately 9%. At March 31, 2015, the Purification Solutions reporting unit had the most significant goodwill balance, in the amount of $439 million. The future growth in the Purification Solutions segment is highly dependent on achieving the expected volumes and margins in the activated carbon based mercury removal business. These volumes and margins are highly dependent on demand for mercury removal products and our successful realization of our anticipated share of volumes in this segment. The expected demand for mercury removal products significantly depends on: (1) the implementation and enforcement of environmental laws and regulations, particularly those that would require U.S. based coal-fired electric utilities to reduce the quantity of air pollutants they release, including mercury, to comply with the Mercury and Air Toxics Standards (MATS) and (2) other factors such as the anticipated usage of activated carbon in the coal-fired energy units. In November 2014, the U.S. Supreme Court agreed to consider whether the Environmental Protection Agency (EPA) appropriately considered costs in determining whether it is necessary and appropriate to regulate hazardous air pollutants emitted by electric utilities, and oral arguments were heard by the Court in March 2015. It is not possible to predict the outcome of the Supreme Court s review of this matter.

33

Table of Contents

The implementation period for the MATS regulations began in April 2015. With this recent implementation, as well as associated customer and industry feedback, we are reassessing our previous estimates for expected growth in volumes, prices and profitability in the Purification Solutions reporting unit. Potential drivers of growth, including the size of the overall mercury removal industry, utility adoption rates, usage levels, and pricing, among others, are still evolving. If we determine, based on these estimates, that the fair value of the Purification Solutions reporting unit is below the carrying amount, we may be required to record an asset impairment charge. With the evolving view of the market, we currently believe that it is reasonably possible that a non-cash impairment charge of up to $350 million may be required. This potential charge, if any, assumes the MATS regulations continue to be implemented on the current schedule or with only a modest delay. If there is a significant delay or change in the MATS requirements as a result of the U.S. Supreme Court s review of the MATS regulations or otherwise, this charge could be higher. This charge may impact goodwill, intangible assets, and long-lived-assets. The potential magnitude of any non-cash charge is preliminary and we expect to complete this analysis during the third quarter of fiscal year 2015. As of March 31, 2015, the carrying value of the Purification Solutions reporting unit was $1.1 billion, which included goodwill and intangibles in the amounts of $439 million and $270 million, respectively, and other long-lived assets.

We use assumptions and estimates in determining the fair value of assets acquired and liabilities assumed in a business combination. The determination of the fair value of intangible assets requires the use of significant judgment with regard to assumptions used in the valuation model. We estimate the fair value of identifiable acquisition-related intangible assets principally based on projections of cash flows that will arise from these assets. The projected cash flows are discounted to determine the fair value of the assets at the dates of acquisition.

Definite-lived intangible assets, which are comprised of customer relationships and developed technologies, are amortized over their estimated useful lives and are reviewed for impairment when indication of potential impairment exists, such as a significant reduction in cash flows associated with the assets. We evaluate indefinite-lived intangible assets, which are comprised of the trademarks of Purification Solutions, for impairment annually or when events occur or circumstances change that may reduce the fair value of the asset below its carrying amount. The annual review is performed as of May 31. We may first perform a qualitative assessment to determine whether it is necessary to perform the quantitative impairment test or bypass the qualitative assessment and proceed directly to performing the quantitative impairment test. The quantitative impairment test is based on discounted estimated future cash flows. The assumptions used to estimate fair value include management s best estimates of future growth rates and discount rates over an estimate of the remaining operating period at the unit of accounting level. These future growth rates depend on achieving the expected volumes and pricing levels of the products of Purification Solutions.

Long-lived Assets

Our long-lived assets primarily include property, plant and equipment, indefinite-lived assets, long-term investments and assets held for rent. The carrying values of long-lived assets are reviewed for impairment whenever events or changes in business circumstances indicate that the carrying amount of an asset may not be recoverable. An asset impairment is recognized when the carrying value of the asset is not recoverable based on the probability-weighted undiscounted estimated future cash flows to be generated by the asset. Our estimates reflect management s assumptions about selling prices, production and sales volumes, costs and market conditions over an estimate of the remaining operating period. If an impairment is indicated, the asset is written down to fair value. If the asset does not have a readily determinable market value, a discounted cash flow model may be used to determine the fair value of the asset. The key inputs to the discounted cash flow would be the same as the undiscounted cash flow noted above, with the addition of the discount rate used. In circumstances when an asset does not have separate identifiable cash flows, an impairment charge is recorded when we no longer intend to use the asset.

To test for impairment of assets we generally use a probability-weighted estimate of the future undiscounted net cash flows of the assets over their remaining lives to determine if the value of the asset is recoverable. Long-lived assets are grouped with other assets and liabilities at the lowest level for which independent identifiable cash flows are determinable.

Property, Plant and Equipment

Property, plant and equipment are recorded at cost. Depreciation of property, plant and equipment is generally calculated using the straight-line method over the estimated useful lives. The depreciable lives for buildings, machinery and equipment, and other fixed assets are twenty to twenty-five years, ten to twenty-five years, and three to twenty-five years, respectively. The cost and accumulated depreciation for property, plant and equipment sold, retired, or otherwise disposed of are removed from the Consolidated Balance Sheets and resulting gains or losses are included in earnings in the Consolidated Statements of Operations. Expenditures for repairs and maintenance are charged to expenses as incurred. Expenditures for major renewals and betterments, which significantly extend the useful lives of existing plant and equipment, are capitalized and depreciated.

Litigation and Contingencies

We are involved in litigation in the ordinary course of business, including personal injury and environmental litigation. After consultation with counsel, as appropriate, we accrue a liability for litigation when it is probable that a liability has been incurred and the amount can be reasonably estimated. The estimated reserves are recorded based on our best estimate of the liability associated with such matters or the low end of the estimated range of liability if we are unable to identify a better estimate within that range. Our best estimate is determined through the evaluation of various information, including claims, settlement offers, demands by government agencies, estimates performed by independent third parties, identification of other responsible parties and an assessment of their ability to contribute, and our prior experience. Litigation is highly uncertain and there is always the possibility of an unusual result in any particular case that may reduce our earnings and cash flows.

The most significant reserves that we have established are for environmental remediation and respirator litigation claims. The amount accrued for environmental matters reflects our assumptions about remediation requirements at the contaminated sites, the nature of the remedies, the outcome of discussions with regulatory agencies and other potentially responsible parties at multi-party sites, and the number and financial viability of other potentially responsible parties. These reserves can be affected by the availability of new information, changes in the assumptions on which the accruals are based, unanticipated government enforcement action or changes in applicable government laws and regulations, which could result in higher or lower costs.

Our current estimate of the cost of our share of existing and future respirator liability claims is based on facts and circumstances existing at this time. Developments that could affect our estimate include, but are not limited to, (i) significant changes in the number of future claims, (ii) changes in the rate of dismissals without payment of pending silica and non-malignant asbestos claims, (iii) significant changes in the average cost of resolving claims, (iv) significant changes in the legal costs of defending these claims, (v) changes in the nature of claims received, (vi) changes in the law and procedure applicable to these claims, (vii) the financial viability of other parties which contribute to the settlement of respirator claims, (viii) a change in the availability of insurance coverage maintained by either the entity from which we acquired the safety respiratory products business or other parties which contribute to the settlement of these claims, or in the indemnity provided by the safety respiratory products business s former owner, (ix) changes in the allocation of costs among the various parties paying legal and settlement costs and (x) a determination that the assumptions that were used to estimate our share of liability are no longer reasonable. We cannot determine the impact of these potential developments on our current estimate of our share of liability for these existing and future claims. Accordingly, the actual amount of these liabilities for existing and future claims could be different than the reserved amount.

Income Taxes

Our business operations are global in nature, and we are subject to taxes in numerous jurisdictions. Tax laws and tax rates vary substantially in these jurisdictions and are subject to change based on the political and economic climate in those countries. We file our tax returns in accordance with our interpretations of each jurisdiction s tax laws.

Significant judgment is required in determining our worldwide provision for income taxes and recording the related tax assets and liabilities. In the ordinary course of our business, there are operational decisions, transactions, facts and circumstances, and calculations which make the ultimate tax determination uncertain. Furthermore, our tax positions are periodically subject to challenge by taxing authorities throughout the world. We have recorded reserves on uncertain tax position for taxes and associated interest and penalties that may become payable in future years as a result of audits by tax authorities. Any significant impact as a result of changes in underlying facts, law, tax rates, tax audit, or review could lead to adjustments to our income tax expense, our effective tax rate, and/or our cash flow.

Table of Contents

We record our tax provision or benefit on an interim basis using an estimated annual effective tax rate. This rate is applied to the current period ordinary income or loss to determine the income tax provision or benefit allocated to the interim period. Losses from jurisdictions for which no benefit can be recognized and the income tax effects of unusual or infrequent items are excluded from the estimated annual effective tax rate and are recognized in the impacted interim period. The estimated annual effective tax rate may be significantly impacted by nondeductible expenses and our projected earnings mix by tax jurisdiction. Adjustments to the estimated annual effective income tax rate are recognized in the period when such estimates are revised.

We record benefits for uncertain tax positions based on an assessment of whether the position is more likely than not to be sustained by the taxing authorities. If this threshold is not met, no tax benefit of the uncertain tax position is recognized. If the threshold is met, the tax benefit that is recognized is the largest amount that is greater than 50% likely of being realized upon ultimate settlement. This analysis presumes the taxing authorities full knowledge of the positions taken and all relevant facts, but does not consider the time value of money. We also accrue for interest and penalties on these uncertain tax positions and include such charges in the income tax provision in the Consolidated Statements of Operations.

Additionally, we have established valuation allowances against a variety of deferred tax assets, including net operating loss carry forwards, foreign tax credits, and other income tax credits. Valuation allowances take into consideration our ability to use these deferred tax assets and reduce the value of such items to the amount that is deemed more likely than not to be recoverable. Our ability to utilize these deferred tax assets is dependent on achieving our forecast of future taxable operating income over an extended period of time. We review our forecast in relation to actual results and expected trends on a quarterly basis. Failure to achieve our operating income targets may change our assessment regarding the recoverability of our net deferred tax assets and such change could result in a valuation allowance being recorded against some or all of our net deferred tax assets. An increase in a valuation allowance would result in additional income tax expense, while a release of valuation allowances in periods when these tax attributes become realizable would reduce our income tax expense.

Inventory Valuation

Inventories are stated at the lower of cost or market. The cost of all carbon black inventories in the U.S. is determined using the last-in, first-out (LIFO) method. Had we used the first-in, first-out (FIFO) method instead of the LIFO method for such inventories, the value of those inventories would have been $40 million and $52 million higher as of March 31, 2015 and September 30, 2014, respectively. The cost of Specialty Fluids inventories is determined using the averag