

EASTMAN CHEMICAL CO

Form 10-Q

July 30, 2007

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549  
FORM 10-Q**

(Mark  
One)

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended June 30, 2007  
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 1-12626

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

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

**62-1539359**  
(I.R.S. employer  
identification no.)

**200 South Wilcox Drive**  
**Kingsport, Tennessee**  
(Address of principal executive offices)

**37660**  
(Zip Code)

Registrant's telephone number, including area code: (423) 229-2000

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES  NO

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

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act) YES  NO

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

<b>Class</b>	<b>Number of Shares Outstanding at June 30, 2007</b>
Common Stock, par value \$0.01 per share	84,045,690

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**UNAUDITED CONSOLIDATED STATEMENTS OF EARNINGS,  
COMPREHENSIVE INCOME AND RETAINED EARNINGS**

(Dollars in millions, except per share amounts)	Second Quarter		First Six Months	
	2007	2006	2007	2006
Sales	\$ 1,895	\$ 1,929	\$ 3,690	\$ 3,732
Cost of sales	1,575	1,579	3,077	3,051
Gross profit	320	350	613	681
Selling, general and administrative expenses	113	113	214	211
Research and development expenses	37	44	73	86
Asset impairments and restructuring charges, net	2	3	23	10
Operating earnings	168	190	303	374
Interest expense, net	15	21	33	41
Other (income) charges, net	(3)	(2)	(6)	(3)
Earnings before income taxes	156	171	276	336
Provision for income taxes	51	57	94	117
Net earnings	\$ 105	\$ 114	\$ 182	\$ 219
<b>Earnings per share</b>				
Basic	\$ 1.24	\$ 1.39	\$ 2.16	\$ 2.68
Diluted	\$ 1.22	\$ 1.37	\$ 2.13	\$ 2.64
<b>Comprehensive Income</b>				
Net earnings	\$ 105	\$ 114	\$ 182	\$ 219
Other comprehensive income (loss)				
Change in cumulative translation adjustment	13	23	9	40
Change in pension and other post employment benefits due to amortization, net of tax	(6)	--	(4)	--
Change in unrealized gains (losses) on investments, net of tax	2	8	1	11
Change in unrealized gains (losses) on derivative instruments, net of tax	(4)	(1)	3	(1)
Total other comprehensive income	5	30	9	50
Comprehensive income	\$ 110	\$ 144	\$ 191	\$ 269
<b>Retained Earnings</b>				
Retained earnings at beginning of period	\$ 2,234	\$ 1,992	\$ 2,186	\$ 1,923
Net earnings	105	114	182	219
Adoption of accounting standards	--	--	8	--
Cash dividends declared	(37)	(36)	(74)	(72)
Retained earnings at end of period	\$ 2,302	\$ 2,070	\$ 2,302	\$ 2,070

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



**CONSOLIDATED STATEMENTS OF FINANCIAL POSITION**

	<b>June 30,</b>	<b>December</b>
(Dollars in millions, except per share amounts)	<b>2007</b>	<b>31,</b>
	(Unaudited)	<b>2006</b>
<b>Assets</b>		
Current assets		
Cash and cash equivalents	\$ 891	\$ 939
Trade receivables, net of allowance of \$12 and \$16	747	682
Miscellaneous receivables	74	72
Inventories	700	682
Other current assets	89	47
Total current assets	2,501	2,422
Properties		
Properties and equipment at cost	8,714	8,844
Less: Accumulated depreciation	5,674	5,775
Net properties	3,040	3,069
Goodwill		
	315	314
Other noncurrent assets	384	368
Total assets	\$ 6,240	\$ 6,173
<b>Liabilities and Stockholders' Equity</b>		
Current liabilities		
Payables and other current liabilities	\$ 1,028	\$ 1,056
Borrowings due within one year	72	3
Total current liabilities	1,100	1,059
Long-term borrowings		
	1,507	1,589
Deferred income tax liabilities	288	269
Post-employment obligations	996	1,084
Other long-term liabilities	179	143
Total liabilities	4,070	4,144
Stockholders' equity		
Common stock (\$0.01 par value – 350,000,000 shares authorized; shares issued – 93,362,017 and 91,579,294 for 2007 and 2006, respectively)	1	1
Additional paid-in capital	549	448
Retained earnings	2,302	2,186
Accumulated other comprehensive loss	(165)	(174)
	2,687	2,461
Less: Treasury stock at cost (9,399,001 shares for 2007 and 8,048,442 shares for 2006)	517	432
Total stockholders' equity	2,170	2,029
Total liabilities and stockholders' equity	\$ 6,240	\$ 6,173

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

**UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Dollars in millions)	First Six Months	
	2007	2006
Cash flows from operating activities		
Net earnings	\$ 182	\$ 219
Adjustments to reconcile net earnings to net cash provided by (used in) operating activities:		
Depreciation and amortization	169	150
Asset impairments	22	8
Provision (benefit) for deferred income taxes	(18)	29
Changes in operating assets and liabilities:		
(Increase) decrease in receivables	(59)	(156)
(Increase) decrease in inventories	(18)	(49)
Increase (decrease) in trade payables	(63)	59
Increase (decrease) in liabilities for employee benefits and incentive pay	(121)	(74)
Other items, net	5	(23)
Net cash provided by operating activities	99	163
Cash flows from investing activities		
Additions to properties and equipment	(198)	(169)
Proceeds from sale of assets and investments	43	11
Additions to capitalized software	(5)	(8)
Other items, net	14	(1)
Net cash (used in) investing activities	(146)	(167)
Cash flows from financing activities		
Net increase (decrease) in commercial paper, credit facility and other borrowings	75	23
Dividends paid to stockholders	(75)	(72)
Treasury stock purchases	(86)	--
Proceeds from stock option exercises and other items	88	24
Net cash provided by (used in) financing activities	2	(25)
Effect of exchange rate changes on cash and cash equivalents	(3)	2
Net change in cash and cash equivalents	( 48)	(27)
Cash and cash equivalents at beginning of period	939	524
Cash and cash equivalents at end of period	\$ 891	\$ 497

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



## NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

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## NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

**1. BASIS OF PRESENTATION**

The accompanying unaudited consolidated financial statements have been prepared by Eastman Chemical Company (the "Company" or "Eastman") in accordance and consistent with the accounting policies stated in the Company's 2006 Annual Report on Form 10-K, except as described below. The Company adopted the provisions of Financial Accounting Standards Board ("FASB") Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* ("FIN 48"), on January 1, 2007. In the opinion of the Company, all normal recurring adjustments necessary for a fair presentation have been included in the unaudited consolidated financial statements. The unaudited consolidated financial statements are prepared in conformity with generally accepted accounting principles ("GAAP") in the United States and, of necessity, include some amounts that are based upon management estimates and judgments. Future actual results could differ from such current estimates. The unaudited consolidated financial statements include assets, liabilities, revenues and expenses of all majority-owned subsidiaries and joint ventures. Eastman accounts for other joint ventures and investments in minority-owned companies where it exercises significant influence on the equity basis. Intercompany transactions and balances are eliminated in consolidation.

The Company has reclassified certain 2006 amounts to conform to the 2007 presentation including the reclassification of segment sales and operating earnings. For additional information, see [Note 14](#) to the Company's unaudited consolidated financial statements.

**2. INVENTORIES**

(Dollars in millions)	June 30, 2007	December 31, 2006
At FIFO or average cost (approximates current cost)		
Finished goods	\$ 635	\$ 660
Work in process	203	206
Raw materials and supplies	326	280
Total inventories	1,164	1,146
LIFO Reserve	(464)	(464)
Total inventories	\$ 700	\$ 682

Inventories valued on the LIFO method were approximately 70% as of June 30, 2007 and 65% as of December 31, 2006 of total inventories.

**3. PAYABLES AND OTHER CURRENT LIABILITIES**

(Dollars in millions)	June 30, 2007	December 31, 2006
Trade creditors	\$ 530	\$ 581
Accrued payrolls, vacation, and variable-incentive compensation	97	126
Accrued taxes	58	