

FULLER H B CO  
Form 10-Q  
March 28, 2011

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 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 February 26, 2011

OR

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

For the transition period from            to

Commission file number: 001-09225

**H.B. FULLER COMPANY**

(Exact name of registrant as specified in its charter)

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

**41-0268370**  
(I.R.S. Employer  
Identification No.)

**1200 Willow Lake Boulevard, St. Paul, Minnesota**  
(Address of principal executive offices)

**55110-5101**  
(Zip Code)

**(651) 236-5900**

(Registrant's telephone number, including area code)

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

Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company)

Smaller reporting company

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

The number of shares outstanding of the Registrant's Common Stock, par value \$1.00 per share, was 49,426,580 as of March 17, 2011.

**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****H.B. FULLER COMPANY AND SUBSIDIARIES****Consolidated Statements of Income**

(In thousands, except per share amounts)

(Unaudited)

|   | 13 Weeks Ended       |                      |
|---|----------------------|----------------------|
|   | February 26,<br>2011 | February 27,<br>2010 |
| <b>Net revenue</b>  | <b>\$ 339,548</b>    | <b>\$ 309,442</b>    |
| Cost of sales   | (242,644)            | (211,763)            |
| <b>Gross profit</b>   | <b>96,904</b>        | 97,679               |
| Selling, general and administrative expenses                                | (75,653)             | (71,448)             |
| Asset impairment charges  | (332)                |                      |
| Other income (expense), net   | 294                  | (63)                 |
| Interest expense  | (2,581)              | (1,948)              |
| <b>Income before income taxes and income from equity method investments</b> | <b>18,632</b>        | 24,220               |
| Income taxes  | (6,285)              | (7,059)              |
| Income from equity method investments                                       | 1,860                | 1,815                |
| <b>Net income including non-controlling interests</b>                       | <b>14,207</b>        | 18,976               |
| Net (income) loss attributable to non-controlling interests                 | 144                  | (24)                 |
| <b>Net income attributable to H.B. Fuller</b>                               | <b>\$ 14,351</b>     | <b>\$ 18,952</b>     |
| <b>Earnings per share attributable to H.B. Fuller common stockholders:</b>  |                      |                      |
| Basic   | \$ 0.29              | \$ 0.39              |
| Diluted   | \$ 0.29              | \$ 0.38              |
| <b>Weighted-average common shares outstanding:</b>                          |                      |                      |
| Basic   | 49,006               | 48,491               |
| Diluted   | 49,877               | 49,494               |
| <b>Dividends declared per common share</b>                                  | <b>\$ 0.070</b>      | <b>\$ 0.068</b>      |
| See accompanying notes to consolidated financial statements.                |                      |                      |

**H.B. FULLER COMPANY AND SUBSIDIARIES****Consolidated Balance Sheets**

(In thousands, except share and per share amounts)

(Unaudited)

|  | February 26,<br>2011 | November 27,<br>2010 |
|--|----------------------|----------------------|
| <b>Assets</b>  |                      |                      |
| <b>Current assets:</b>   |                      |                      |
| Cash and cash equivalents  | \$ 121,938           | \$ 133,277           |
| Trade receivables (net of allowances - \$5,370 and \$5,895, for February 26, 2011 and November 27, 2010, respectively) | 226,835              | 221,020              |
| Inventories  | 143,836              | 121,621              |
| Other current assets   | 58,416               | 57,699               |
| <b>Total current assets</b>  | <b>551,025</b>       | <b>533,617</b>       |
| Property, plant and equipment  | 821,245              | 806,804              |
| Accumulated depreciation   | (568,559)            | (555,729)            |
| <b>Property, plant and equipment, net</b>  | <b>252,686</b>       | <b>251,075</b>       |
| Goodwill   | 112,392              | 108,970              |
| Other intangibles, net   | 129,266              | 131,517              |
| Other assets   | 128,352              | 128,278              |
| <b>Total assets</b>  | <b>\$ 1,173,721</b>  | <b>\$ 1,153,457</b>  |
| <b>Liabilities and total equity</b>  |                      |                      |
| <b>Current liabilities:</b>  |                      |                      |
| Notes payable  | \$ 23,573            | \$ 27,243            |
| Current maturities of long-term debt   | 22,500               | 22,500               |
| Trade payables   | 122,871              | 102,107              |
| Accrued compensation   | 33,489               | 45,645               |
| Income taxes payable   | 5,168                | 4,931                |
| Other accrued expenses   | 22,103               | 28,907               |
| <b>Total current liabilities</b>   | <b>229,704</b>       | <b>231,333</b>       |
| Long-term debt, excluding current maturities   | 193,096              | 200,978              |
| Accrued pension liabilities  | 39,588               | 42,788               |
| Other liabilities  | 44,132               | 43,968               |
| <b>Total liabilities</b>   | <b>506,520</b>       | <b>519,067</b>       |
| Commitments and contingencies  |                      |                      |
| <b>Equity:</b>   |                      |                      |
| H.B. Fuller stockholders' equity:  |                      |                      |
| Preferred stock (no shares outstanding) Shares authorized  | 10,045,900           |                      |

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|  |                     |              |
|--|---------------------|--------------|
| Common stock, par value \$1.00 per share, Shares authorized 160,000,000, Shares outstanding 49,419,071 and 49,194,251, for February 26, 2011 and November 27, 2010, respectively | <b>49,419</b>       | 49,194       |
| Additional paid-in capital   | <b>25,701</b>       | 22,701       |
| Retained earnings  | <b>657,460</b>      | 646,596      |
| Accumulated other comprehensive income (loss)  | <b>(67,700)</b>     | (86,557)     |
| Total H.B. Fuller stockholders' equity   | <b>664,880</b>      | 631,934      |
| Non-controlling interests  | <b>2,321</b>        | 2,456        |
| <b>Total equity</b>  | <b>667,201</b>      | 634,390      |
| <b>Total liabilities and total equity</b>  | <b>\$ 1,173,721</b> | \$ 1,153,457 |

See accompanying notes to consolidated financial statements.

**H.B. FULLER COMPANY AND SUBSIDIARIES****Consolidated Statements of Total Equity**

(In thousands)

(Unaudited)

|   | H.B. Fuller Company Shareholders |                                  |                      |  |                                  | Total      |
|---|----------------------------------|----------------------------------|----------------------|--|----------------------------------|------------|
|   | Common<br>Stock                  | Additional<br>Paid-in<br>Capital | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Income (Loss) | Non-<br>Controlling<br>Interests |            |
| <b>Balance at November 28, 2009</b>                               | \$ 48,658                        | \$ 12,309                        | \$ 589,451           | \$ (59,064)  | \$ 2,888                         | \$ 594,242 |
| Net income including non-controlling interests                    |                                  |                                  | 70,877               |  | (458)                            | 70,419     |
| Foreign currency translation                                      |                                  |                                  |                      | (28,666)   | 26                               | (28,640)   |
| Medicare Part D Subsidy tax adjustment                            |                                  |                                  |                      | (1,484)  |                                  | (1,484)    |
| Defined benefit pension plans adjustment, net of tax of \$(1,523) |                                  |                                  |                      | 2,626  |                                  | 2,626      |
| Interest rate swap, net of tax                                    |                                  |                                  |                      | 31   |                                  | 31         |
| <b>Comprehensive income</b>                                       |                                  |                                  |                      |  |                                  | 42,952     |
| Dividends   |                                  |                                  | (13,732)             |  |                                  | (13,732)   |
| Stock option exercises  | 358                              | 3,592                            |                      |  |                                  | 3,950      |
| Share-based compensation plans other, net                         | 196                              | 6,650                            |                      |  |                                  | 6,846      |
| Tax benefit on share-based compensation plans                     |                                  | 509                              |                      |  |                                  | 509        |
| Repurchases of common stock                                       | (18)                             | (359)                            |                      |  |                                  | (377)      |
| <b>Balance at November 27, 2010</b>                               | 49,194                           | 22,701                           | 646,596              | (86,557)   | 2,456                            | 634,390    |
| Net income including non-controlling interests                    |                                  |                                  | 14,351               |  | (144)                            | 14,207     |
| Foreign currency translation                                      |                                  |                                  |                      | 17,400   | 9                                | 17,409     |
| Defined benefit pension plans adjustment, net of tax of \$833     |                                  |                                  |                      | 1,447  |                                  | 1,447      |
| Interest rate swaps, net of tax                                   |                                  |                                  |                      | 10   |                                  | 10         |
| <b>Comprehensive income</b>                                       |                                  |                                  |                      |  |                                  | 33,073     |
| Dividends   |                                  |                                  | (3,487)              |  |                                  | (3,487)    |
| Stock option exercises  | 308                              | 4,495                            |                      |  |                                  | 4,803      |
| Share-based compensation plans other, net                         | 56                               | 1,290                            |                      |  |                                  | 1,346      |
| Tax benefit on share-based compensation plans                     |                                  | 200                              |                      |  |                                  | 200        |
| Repurchases of common stock                                       | (139)                            | (2,985)                          |                      |  |                                  | (3,124)    |
| <b>Balance at February 26, 2011</b>                               | \$ 49,419                        | \$ 25,701                        | \$ 657,460           | \$ (67,700)  | \$ 2,321                         | \$ 667,201 |

See accompanying notes to consolidated financial statements.

**H.B. FULLER COMPANY AND SUBSIDIARIES****Consolidated Statements of Cash Flows**

(In thousands)

(Unaudited)

|   | 13 Weeks Ended    |                   |
|---|-------------------|-------------------|
|   | February 26, 2011 | February 27, 2010 |
| <b>Cash flows from operating activities:</b>  |                   |                   |
| Net income including non-controlling interests  | \$ 14,207         | \$ 18,976         |
| Adjustments to reconcile net income including non-controlling interests to net cash provided by operating activities: |                   |                   |
| Depreciation  | 7,580             | 7,440             |
| Amortization  | 2,486             | 3,011             |
| Deferred income taxes   | 967               | 387               |
| Income from equity method investments   | (1,860)           | (1,815)           |
| Share-based compensation  | 1,790             | 1,929             |
| Excess tax benefit from share-based compensation  | (200)             | (44)              |
| Asset impairment charges  | 332               |                   |
| Change in assets and liabilities, net of effects of acquisitions:   |                   |                   |
| Trade receivables, net  | (2,461)           | 13,395            |
| Inventories   | (20,144)          | (18,934)          |
| Other assets  | 295               | (381)             |
| Trade payables  | 19,265            | (2,014)           |
| Accrued compensation  | (12,731)          | (11,867)          |
| Other accrued expenses  | (7,137)           | (710)             |
| Income taxes payable  | (171)             | 5,857             |
| Accrued / prepaid pensions  | (3,166)           | (4,761)           |
| Other liabilities   | (403)             | (4,560)           |
| Other   | 2,818             | (4,797)           |
| <b>Net cash provided by operating activities</b>  | <b>1,467</b>      | <b>1,112</b>      |
| <b>Cash flows from investing activities:</b>  |                   |                   |
| Purchased property, plant and equipment   | (6,122)           | (9,395)           |
| Proceeds from sale of property, plant and equipment   | 126               | 169               |
| <b>Net cash used in investing activities</b>  | <b>(5,996)</b>    | <b>(9,226)</b>    |
| <b>Cash flows from financing activities:</b>  |                   |                   |
| Proceeds from long-term debt  | 33,000            | 273,000           |
| Repayment of long-term debt   | (38,625)          | (211,000)         |
| Net proceeds from notes payable   | (3,661)           | 3,923             |
| Dividends paid  | (3,452)           | (3,326)           |
| Proceeds from stock options exercised   | 4,803             | 1,210             |
| Excess tax benefit from share-based compensation  | 200               | 44                |
| Repurchases of common stock   | (3,124)           | (376)             |
| <b>Net cash provided by (used in) financing activities</b>  | <b>(10,859)</b>   | <b>63,475</b>     |
| Effect of exchange rate changes   | 4,049             | (6,541)           |
| <b>Net change in cash and cash equivalents</b>  | <b>(11,339)</b>   | <b>48,820</b>     |
| Cash and cash equivalents at beginning of period  | 133,277           | 100,154           |
| <b>Cash and cash equivalents at end of period</b>   | <b>\$ 121,938</b> | <b>\$ 148,974</b> |

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Supplemental disclosure of cash flow information:

|                                   |          |          |
|-----------------------------------|----------|----------|
| Dividends paid with company stock | \$ 35    | \$ 15    |
| Cash paid for interest            | \$ 4,785 | \$ 2,296 |
| Cash paid for income taxes        | \$ 1,559 | \$ 3,355 |

See accompanying notes to consolidated financial statements.



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

**Notes to Consolidated Financial Statements**

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

(Unaudited)

**Note 1: Accounting Policies**

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

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses, and related disclosures at the date of the financial statements and during the reporting period. Actual results could differ from these estimates. These unaudited interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended November 27, 2010 as filed with the Securities and Exchange Commission.

**Recently Adopted Accounting Pronouncements:**

On November 28, 2010, the beginning of our fiscal 2011, we adopted the new guidance in ASC Topic 605, Revenue Recognition, relating to the accounting for revenue arrangements involving multiple deliverables. The updates require companies to allocate revenue in arrangements involving multiple deliverables based on the estimated selling price of each deliverable, even though such deliverables are not sold separately either by the company itself or other vendors. This guidance eliminates the requirement that all undelivered elements must have objective and reliable evidence of fair value before a company can recognize the portion of the overall arrangement fee that is attributable to items that already have been delivered. As a result, the new guidance may allow some companies to recognize revenue on transactions that involve multiple deliverables earlier than under previous requirements. The adoption of this standard did not have a material impact on our consolidated financial statements.

**Note 2: Acquisitions**

**Revertex Finewaters Sdn. Bhd.** On June 2, 2010, we acquired the outstanding shares of Revertex Finewaters Sdn. Bhd., a supplier of adhesives in Malaysia and Southeast Asia, based outside Kuala Lumpur, Malaysia. The acquisition further strengthens our market position in Southeast Asia and expands our geographic presence and customer portfolio in the region. The acquisition was a stock purchase and therefore encompasses all Revertex Finewaters business operations. The acquisition was recorded in our Asia Pacific operating segment.

The purchase price of \$26,768, which was net of cash acquired of \$557, was funded through existing cash. We also incurred acquisition related costs of approximately \$498, which were recorded as selling, general and administrative expenses in the consolidated statements of income.

Of the \$11,144 of acquired intangibles, \$7,271 was assigned to customer relationships with an expected life of 12 years, \$2,978 was assigned to trademarks with an expected life of 15 years and \$895 was assigned to non-competition agreements with an expected life of 4 years.

**Nordic Adhesive Technology:** On April 20, 2009 we acquired the outstanding shares of Nordic Adhesive Technology GmbH, a developer and manufacturer of flexible packaging adhesives, based in Buxtehude, Germany. The acquisition complements our existing product line, enhances our applications knowledge and enables us to expand our presence in the flexible packaging segment of the adhesives industry. The acquisition was a stock purchase and therefore encompasses all Nordic Adhesive Technology business operations. Intangible assets identified were customer lists, technology, trademarks and non-competition agreements.

The original purchase price of \$4,175, which was net of cash acquired of \$370, was funded through existing cash. We also incurred \$295 of direct external costs for legal and due diligence expenses. The acquisition was recorded in our EIMEA (Europe, India, Middle East and Africa) operating segment.

The former shareholders of Nordic Adhesive Technology are entitled to an earn-out of up to 2,600, over the first three years, based on certain financial performance criteria. The first earn-out was based on financial performance for a period from April 2009 to April 2010. According to the terms of the agreement, the first earn-out period resulted in the former shareholders earning 608 or approximately \$805. Because this acquisition occurred prior to the new rules on accounting for business combinations, this amount was considered additional purchase price, which increased goodwill. There are two remaining earn-out periods that could result in additional payments of up to 1,992 which would also be considered additional purchase price. No amounts have been accrued for the remaining two earn-out periods as the contingency has not been resolved and additional consideration is not distributable as of the end of the first quarter of 2011.

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

**Overview:** We have various share-based compensation programs, which provide for equity awards including stock options, restricted stock and deferred compensation. These equity awards fall under several plans and are described in detail in our Annual Report filed on Form 10-K as of November 27, 2010.

**Grant-Date Fair Value:** We use the Black-Scholes option-pricing model to calculate the grant-date fair value of an award. The fair value of options granted during the 13 weeks ended February 26, 2011 and February 27, 2010, respectively, were calculated using the following assumptions:

|                                       | 13 Weeks Ended    |                   |
|---------------------------------------|-------------------|-------------------|
|                                       | February 26, 2011 | February 27, 2010 |
| Expected life (in years)              | 4.75              | 5.00              |
| Weighted-average expected volatility  | 52.30%            | 50.80%            |
| Expected volatility                   | 52.30%            | 50.80%            |
| Risk-free interest rate               | 1.94%             | 2.14%             |
| Expected dividend yield               | 1.29%             | 1.35%             |
| Weighted-average fair value of grants | \$ 9.23           | \$ 8.48           |

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

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

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

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

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

Total share-based compensation expense of \$1,790 and \$1,929 was included in our Consolidated Statements of Income for the 13 weeks ended February 26, 2011 and February 27, 2010, respectively. No share-based compensation was capitalized. All share-based compensation was recorded as selling, general and administrative expense. For the 13 weeks ended February 26, 2011 there was \$200 of excess tax benefit recognized. For the 13 weeks ended February 27, 2010, there was \$44 of excess tax benefit recognized.

As of February 26, 2011, there was \$8,255 of unrecognized compensation costs related to unvested stock option awards, which is expected to be recognized over a weighted-average period of 2.2 years. Unrecognized compensation costs related to unvested restricted stock awards was \$6,680, which is expected to be recognized over a weighted-average period of 1.4 years.

### Share-based Activity

A summary of option activity as of February 26, 2011 and changes during the 13 weeks then ended is presented below:

|                                  | Options   | Weighted-Average Exercise Price |
|----------------------------------|-----------|---------------------------------|
| Outstanding at November 27, 2010 | 2,820,468 | \$ 18.25                        |
| Granted                          | 452,514   | 22.27                           |
| Exercised                        | (308,455) | 15.57                           |
| Forfeited or Cancelled           | (233,018) | 19.19                           |
| Outstanding at February 26, 2011 | 2,731,509 | \$ 19.14                        |

The fair value of options granted during the 13 weeks ended February 26, 2011 and February 27, 2010 were \$4,174 and \$4,720, respectively. Total intrinsic value of options exercised during the 13 weeks ended February 26, 2011 and February 27, 2010 were \$2,099 and \$774, respectively. Intrinsic value is the difference between our closing stock price on the respective trading day and the exercise price, multiplied by the number of options exercised. Proceeds received from option exercises during the 13 weeks ended February 26, 2011 and February 27, 2010 were \$4,803 and \$1,210, respectively.

A summary of nonvested restricted stock activity as of February 26, 2011, and changes during the 13 weeks then ended is presented below:

|                                | Units    | Shares   | Total     | Weighted-Average Grant Date Fair Value | Weighted-Average Remaining Contractual Life (in Years) |
|--------------------------------|----------|----------|-----------|--|--|
| Nonvested at November 27, 2010 | 111,940  | 365,829  | 477,769   | \$ 19.17                               | 1.7  |
| Granted                        | 77,847   | 112,542  | 190,389   | 22.27                                  | 2.9  |
| Vested                         | (35,133) | (82,058) | (117,191) | 21.61                                  |  |
| Forfeited                      | (6,532)  | (90,154) | (96,686)  | 18.61                                  | 1.8  |
| Nonvested at February 26, 2011 | 148,122  | 306,159  | 454,281   | \$ 20.89                               | 1.4  |

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Total fair value of restricted stock vested during the 13 weeks ended February 26, 2011 and February 27, 2010 was \$2,532 and \$1,436, respectively. The total fair value of nonvested restricted stock at February 26, 2011 was \$8,801.

We repurchased 29,142 and 17,804 restricted stock shares during the 13 weeks ended February 26, 2011 and February 27, 2010, respectively, in conjunction with restricted stock vestings. The repurchases relate to statutory minimum tax withholding. We expect approximately 17,000 additional shares for statutory minimum tax withholding to be repurchased in fiscal 2011.

We have a Directors' Deferred Compensation plan that allows non-employee directors to defer all or a portion of their retainer and meeting fees in a number of investment choices, including units representing shares of our common stock. We also have a Key Employee Deferred Compensation Plan that allows key employees to defer a portion of their eligible compensation in a number of investment choices, including units, representing shares of our common stock. We provide a 10 percent match on deferred compensation invested into units, representing shares of our common stock. A summary of deferred compensation unit activity as of February 26, 2011, and changes during the 13 weeks then ended is presented below:

|  | Non-employee   |               | Total          |
|--|----------------|---------------|----------------|
|  | Directors      | Employees     |                |
| Units outstanding November 27, 2010        | 277,345        | 88,798        | 366,143        |
| Participant contributions                  | 4,659          | 1,935         | 6,594          |
| Company match contributions                | 845            | 272           | 1,117          |
| Payouts                                    |                | (4,341)       | (4,341)        |
| <b>Units outstanding February 26, 2011</b> | <b>282,849</b> | <b>86,664</b> | <b>369,513</b> |

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

#### Note 4: Earnings Per Share

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

|   | 13 Weeks Ended       |                      |
|---|----------------------|----------------------|
|   | February 26,<br>2011 | February 27,<br>2010 |
| Weighted-average common shares - basic                                | <b>49,006,026</b>    | 48,490,604           |
| Equivalent shares from share-based compensations plans                | <b>870,983</b>       | 1,003,731            |
| <b>Weighted-average common and common equivalent shares - diluted</b> | <b>49,877,009</b>    | 49,494,335           |

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

Options to purchase 966,011 and 1,200,223 shares of common stock at the weighted-average exercise price of \$24.66 and \$23.38 for the 13 week periods ended February 26, 2011 and February 27, 2010, respectively, were excluded from the diluted earnings per share calculations because they were antidilutive.

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

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

|   | Total       | February 26, 2011           |                              |
|---|-------------|-----------------------------|------------------------------|
|   |             | H.B. Fuller<br>Stockholders | Non-controlling<br>Interests |
| Foreign currency translation adjustment                           | \$ 67,779   | \$ 67,757                   | \$ 22                        |
| Interest rate swap, net of taxes of \$80                          | (208)       | (208)                       |                              |
| Defined benefit pension plans adjustment net of taxes of \$74,635 | (135,249)   | (135,249)                   |                              |
| Total accumulated other comprehensive income (loss)               | \$ (67,678) | \$ (67,700)                 | \$ 22                        |

  

|   | Total       | November 27, 2010           |                              |
|---|-------------|-----------------------------|------------------------------|
|   |             | H.B. Fuller<br>Stockholders | Non-controlling<br>Interests |
| Foreign currency translation adjustment                           | \$ 50,370   | \$ 50,357                   | \$ 13                        |
| Interest rate swap, net of taxes of \$84                          | (218)       | (218)                       |                              |
| Medicare Part D Subsidy tax adjustment                            | (1,484)     | (1,484)                     |                              |
| Defined benefit pension plans adjustment net of taxes of \$75,468 | (135,212)   | (135,212)                   |                              |
| Total accumulated other comprehensive income (loss)               | \$ (86,544) | \$ (86,557)                 | \$ 13                        |

**Note 6: Components of Net Periodic Cost (Benefit) related to Pension and Other Postretirement Benefit Plans**

|                              | 13 Weeks Ended February 26, 2011 and February 27, 2010 |          |                |         |                               |         |
|------------------------------|--|----------|----------------|---------|-------------------------------|---------|
|                              | Pension Benefits                                       |          |                |         | Other Postretirement Benefits |         |
|                              | U.S. Plans   |          | Non-U.S. Plans |         | 2011                          | 2010    |
| Net periodic cost (benefit): | 2011   | 2010     | 2011           | 2010    | 2011                          | 2010    |
| Service cost                 | \$ 1,371   | \$ 1,374 | \$ 267         | \$ 269  | \$ 129                        | \$ 135  |
| Interest cost                | 4,281  | 4,276    | 1,753          | 1,838   | 669                           | 731     |
| Expected return on assets    | (6,372)  | (6,558)  | (1,903)        | (2,052) | (772)                         | (684)   |
| Amortization:                |  |          |                |         |                               |         |
| Prior service cost           | 17   | 17       | (1)            | (1)     | (1,173)                       | (1,159) |
| Actuarial (gain)/ loss       | 1,501  | 617      | 655            | 644     | 1,483                         | 1,583   |
| Net periodic cost (benefit)  | \$ 798   | \$ (274) | \$ 771         | \$ 718  | \$ 336                        | \$ 606  |

In the first quarter of 2011, we contributed \$3,039 to our U.K. pension plan based on statutory requirements.

**Note 7: Inventories**

The composition of inventories follows:

|                | February 26,<br>2011 | November 28,<br>2010 |
|----------------|----------------------|----------------------|
| Raw materials  | \$ 77,999            | \$ 64,404            |
| Finished goods | 85,551               | 76,450               |
| LIFO reserve   | (19,714)             | (19,233)             |

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|                   |            |            |
|-------------------|------------|------------|
| Total inventories | \$ 143,836 | \$ 121,621 |
|-------------------|------------|------------|

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**Note 8: Financial Instruments**

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

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

We enter into derivative contracts with a group of investment grade multinational commercial banks. Each of these banks is a participant in our revolving credit facility. We evaluate the credit quality of each of these banks on a periodic basis as warranted.

Foreign currency derivative instruments outstanding are not designated as hedges for accounting purposes, the gains and losses related to mark-to-market adjustments are recognized as other income or expense in the income statement during the periods in which the derivative instruments are outstanding. See Note 13, Fair Value Measurements, for the fair value amounts of these derivative instruments.

As of February 26, 2011, we had forward foreign currency contracts maturing between March 1, 2011 and November 1, 2011. The mark-to-market effect associated with these contracts, on a net basis, was a gain of \$1,867 at February 26, 2011. These gains were largely offset by the underlying transaction gains and losses resulting from the foreign currency exposures for which these contracts relate.

We have interest rate swap agreements to convert \$75,000 of our Senior Notes to variable interest rates. The change in fair value of the Senior Notes, attributable to the change in the risk being hedged, was a liability of \$1,846 at February 26, 2011 and was included in long-term debt in the consolidated balance sheet. The fair values of the swaps in total were an asset of \$1,420 at February 26, 2011 and were included in other assets in the consolidated balance sheet. The swaps were designated for hedge accounting treatment. The hedge ineffectiveness calculation as of February 26, 2011 resulted in additional expense of \$219 for the quarter as the fair value of the interest rate swaps decreased by more than the change in the fair value of the Senior Notes attributable to the change in the risk being hedged.

Concentrations of credit risk with respect to trade accounts receivable are limited due to the large number of entities in the customer base and their dispersion across many different industries and countries. As of February 26, 2011, there were no significant concentrations of credit risk.

**Note 9: Commitments and Contingencies**

**Environmental Matters.** From time to time, we are identified as a potentially responsible party (PRP) under the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) and/or similar state laws that impose liability for costs relating to the clean up of contamination resulting from past spills, disposal or other release of hazardous substances. We are also subject to similar laws in some of the countries where current and former facilities are located. Our environmental, health and safety department monitors compliance with applicable laws on a global basis.

Currently we are involved in various environmental investigations, clean up activities and administrative proceedings and lawsuits. In particular, we are currently deemed a PRP in conjunction with numerous other parties, in a number of government enforcement actions associated with hazardous waste sites. As a PRP, we may be required to pay a share of the costs of investigation and clean up of these sites. In addition, we are engaged in environmental remediation and monitoring efforts at a number of current and former operating facilities, including remediation of environmental contamination at the Sorocaba, Brazil facility. Soil and water samples were collected on and around the Sorocaba facility, and test results indicated that certain contaminants, including carbon tetrachloride and other solvents, exist in the soil at the Sorocaba facility and in the groundwater at both the Sorocaba facility and some neighboring properties. We are continuing to work with Brazilian regulatory authorities to

implement and operate a remediation system at the site. As of February 26, 2011, \$1,092 was recorded as a liability for expected remediation expenses remaining for this site. Depending on the results of the testing of our current remediation actions, we may be required to record additional liabilities related to remediation costs at the Sorocaba facility.

From time to time, we become aware of compliance matters relating to, or receive notices from, federal, state or local entities regarding possible or alleged violations of environmental, health or safety laws and regulations. We review the circumstances of each individual site, considering the number of parties involved, the level of potential liability or contribution of us relative to the other parties, the nature and magnitude of the hazardous substances involved, the method and extent of remediation, the estimated legal and consulting expense with respect to each site and the time period over which any costs would likely be incurred. To the extent we can reasonably estimate the amount of our probable liabilities for environmental matters, we establish a financial provision. As of February 26, 2011, we had reserved \$2,617, which represents our best estimate of probable liabilities with respect to environmental matters, inclusive of the accrual related to the Sorocaba facility as described above. However, the full extent of our future liability for environmental matters is difficult to predict because of uncertainty as to the cost of investigation and clean up of the sites, our responsibility for such hazardous substances and the number of and financial condition of other potentially responsible parties.

While uncertainties exist with respect to the amounts and timing of the ultimate environmental liabilities, based on currently available information, we do not believe that these matters, individually or in aggregate, will have a material adverse effect on our long-term financial condition. However, adverse developments and/or periodic settlements could negatively impact the results of operations or cash flows in one or more future periods.

**Other Legal Proceedings.** From time to time and in the ordinary course of business, we are a party to, or a target of, lawsuits, claims, investigations and proceedings, including product liability, personal injury, contract, patent and intellectual property, health and safety and employment matters. While we are unable to predict the outcome of these matters, we do not believe, based upon currently available information, that the ultimate resolution of any pending matter, individually or in aggregate, including the asbestos litigation described in the following paragraphs, will have a material adverse effect on our long-term financial condition. However, adverse developments and/or periodic settlements could negatively impact the results of operations or cash flows in one or more future periods.

We have been named as a defendant in lawsuits in which plaintiffs have alleged injury due to products containing asbestos manufactured more than 25 years ago. The plaintiffs generally bring these lawsuits against multiple defendants and seek damages (both actual and punitive) in very large amounts. In many cases, plaintiffs are unable to demonstrate that they have suffered any compensable injuries or that the injuries suffered were the result of exposure to products manufactured by us. We are typically dismissed as a defendant in such cases without payment. If the plaintiff presents evidence indicating that compensable injury occurred as a result of exposure to our products, the case is generally settled for an amount that reflects the seriousness of the injury, the length, intensity and character of exposure to products containing asbestos, the number and solvency of other defendants in the case, and the jurisdiction in which the case has been brought.

A significant portion of the defense costs and settlements in asbestos-related litigation continues to be paid by third parties, including indemnification pursuant to the provisions of a 1976 agreement under which we acquired a business from a third party. Historically, this third party routinely defended all cases tendered to it and paid settlement amounts resulting from those cases. In the 1990s, the third party sporadically reserved its rights, but continued to defend and settle all asbestos-related claims tendered to it by us. In 2002, the third party rejected the tender of certain cases and indicated it would seek contributions for past defense costs, settlements and judgments. However, this third party is defending and paying settlement amounts, under a reservation of rights, in most of the asbestos cases tendered to the third party. As discussed below, during the fourth quarter of 2007, we and a group of other defendants, including the third party obligated to indemnify us against certain asbestos-related claims, entered into negotiations with certain law firms to settle a number of asbestos-related lawsuits and claims.

In addition to the indemnification arrangements with third parties, we have insurance policies that generally provide coverage for asbestos liabilities (including defense costs). Historically, insurers have paid a significant portion of our defense costs and settlements in asbestos-related litigation. However, certain of our insurers are insolvent. We have entered into cost-sharing agreements with our insurers that provide for the allocation of defense costs and, in some cases, settlements and judgments, in asbestos-related lawsuits. Under these agreements, we are required in some cases to fund a share of settlements and judgments allocable to years in which the responsible insurer is insolvent. In addition, to delineate our rights under certain insurance policies, in October 2009, we commenced a declaratory judgment action against one of our insurers in the United States District Court for the District of Minnesota. Additional insurers have been brought into the action to address issues related to the scope of their coverage. The lawsuit is in its early stages.



As referenced above, during the fourth quarter of 2007, we and a group of other defendants entered into negotiations with certain law firms to settle a number of asbestos-related lawsuits and claims over a period of years. In total, we had expected to contribute up to \$4,114, based on a present value calculation, towards the settlement amounts to be paid to the claimants in exchange for full releases of claims. Of this amount, our insurers had committed to pay \$2,043 based on the probable liability of \$4,114. Our contributions toward settlements from the time of the agreement through the end of fiscal year 2010 were \$1,674 with insurers paying \$892 of that amount. Based on this experience we reduced our reserves in the fourth quarter of 2010 to an undiscounted amount of \$800 with insurers expected to pay \$510. During the first quarter of 2011 we contributed another \$210 toward settlements with insurers contributing \$134 of that amount. This reduced our reserves for this agreement to \$590 with an insurance receivable of \$376. These amounts represent our best estimate for the settlement amounts yet to be paid related to this agreement. Our reserve is recorded on an undiscounted basis.

In addition to the group settlement referenced above, a summary of the number of and settlement amounts for asbestos-related lawsuits and claims is as follows:

|  | <b>13 Weeks<br/>Ended<br/>February 26, 2011</b> | <b>13 Weeks<br/>Ended<br/>February 27, 2010</b> |
|--|---|---|
| Lawsuits and claims settled                            | 2   | 2   |
| Settlement amounts                                     | \$ 180  | \$ 398  |
| Insurance payments received or expected to be received | \$ 137  | \$ 322  |

We do not believe that it would be meaningful to disclose the aggregate number of asbestos-related lawsuits filed against us because relatively few of these lawsuits are known to involve exposure to asbestos-containing products that we manufactured. Rather, we believe it is more meaningful to disclose the number of lawsuits that are settled and result in a payment to the plaintiff.

To the extent we can reasonably estimate the amount of our probable liabilities for pending asbestos-related claims, we establish a financial provision and a corresponding receivable for insurance recoveries. As of February 26, 2011, our probable liabilities and insurance recoveries related to asbestos claims were \$743 and \$521, respectively. We have concluded that it is not possible to reasonably estimate the cost of disposing of other asbestos-related claims (including claims that might be filed in the future) due to our inability to project future events. Future variables include the number of claims filed or dismissed, proof of exposure to our products, seriousness of the alleged injury, the number and solvency of other defendants in each case, the jurisdiction in which the case is brought, the cost of disposing of such claims, the uncertainty of asbestos litigation, insurance coverage and indemnification agreement issues, and the continuing solvency of certain insurance companies.

Based on currently available information, we do not believe that asbestos-related litigation, individually or in aggregate, will have a material adverse effect on our long-term financial condition. However, adverse developments and/or periodic settlements in such litigation could negatively impact the results of operations or cash flows in one or more future quarters.

In addition to product liability claims discussed above, we are involved in other claims or legal proceedings related to our products, which we believe are not out of the ordinary in a business of the type and size in which we are engaged.

#### **Note 10: Operating Segments**

We evaluate the performance of each of our operating segments based on operating income, which is defined as gross profit less selling, general and administrative (SG&A) expenses. Corporate expenses are fully allocated to each operating segment.

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

|               | 13 Weeks Ended    |                       |                  |                   |                       |                  |
|---------------|-------------------|-----------------------|------------------|-------------------|-----------------------|------------------|
|               | February 26, 2011 |                       |                  | February 27, 2010 |                       |                  |
|               | Trade Revenue     | Inter-Segment Revenue | Operating Income | Trade Revenue     | Inter-Segment Revenue | Operating Income |
| North America | \$ 134,926        | \$ 11,454             | \$ 14,881        | \$ 127,067        | \$ 9,325              | \$ 17,203        |
| EIMEA         | 100,806           | 2,954                 | 1,946            | 94,018            | 2,131                 | 4,110            |
| Latin America | 59,896            |                       | 3,358            | 55,294            | 12                    | 2,852            |
| Asia Pacific  | 43,920            | 2,814                 | 1,066            | 33,063            | 1,597                 | 2,066            |
| <b>Total</b>  | <b>\$ 339,548</b> |                       | <b>\$ 21,251</b> | <b>\$ 309,442</b> |                       | <b>\$ 26,231</b> |

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

|   | 13 Weeks Ended    |                   |
|---|-------------------|-------------------|
|   | February 26, 2011 | February 27, 2010 |
| Operating income  | \$ 21,251         | \$ 26,231         |
| Asset impairment charges  | (332)             |                   |
| Other income (expense), net   | 294               | (63)              |
| Interest expense  | (2,581)           | (1,948)           |
| <b>Income before income taxes and income from equity method investments</b> | <b>\$ 18,632</b>  | <b>\$ 24,220</b>  |

**Note 11: Income Taxes**

As of February 26, 2011, we had a \$7,397 liability recorded under FASB ASC 740 Income Taxes for gross unrecognized tax benefits (excluding interest). As of February 26, 2011, we had accrued \$1,497 of net interest and penalties relating to unrecognized tax benefits. During the first quarter of 2011 our recorded liability for unrecognized tax benefits, net, increased by \$1,531 principally as a result of audit activity in various foreign jurisdictions. Of this amount, \$920 was recognized as a discrete tax expense in the first quarter.

**Note 12: Goodwill**

A summary of goodwill activity for the first three months of 2011 is presented below:

|                                     |                   |
|-------------------------------------|-------------------|
| Balance at November 27, 2010        | \$ 108,970        |
| Currency impact                     | 3,422             |
| <b>Balance at February 26, 2011</b> | <b>\$ 112,392</b> |

**Note 13: Fair Value Measurements**

The following table presents information about our financial assets and liabilities that are measured at fair value on a recurring basis as of February 26, 2011, and indicates the fair value hierarchy of the valuation techniques utilized to determine such fair value. The hierarchy is broken down into three levels. Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 inputs include data points that are observable such as quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, and inputs (other than quoted prices) such as interest rates and yield curves that are observable for the asset or liability, either directly or indirectly. Level 3 inputs are unobservable data points for the asset or liability, and include

situations where there is little, if any, market activity for the asset or liability.

| Description            | February 26,<br>2011 | Fair Value Measurements Using: |         |         | Total<br>Gains (Losses) |
|------------------------|----------------------|--------------------------------|---------|---------|-------------------------|
|                        |                      | Level 1                        | Level 2 | Level 3 |                         |
| <b>Assets:</b>         |                      |                                |         |         |                         |
| Marketable securities  | \$ 43,680            | \$ 43,680                      | \$      | \$      | \$                      |
| Derivative assets      | 2,198                |                                | 2,198   |         |                         |
| Interest rate swaps    | 1,420                |                                | 1,420   |         |                         |
| <b>Liabilities:</b>    |                      |                                |         |         |                         |
| Derivative liabilities | \$ 331               | \$                             | \$ 331  | \$      | \$                      |

**Note 14: Share Repurchase Program**

On September 30, 2010, the Board of Directors authorized a new share repurchase program of up to \$100,000 of our outstanding common shares. Under the program, we are authorized to repurchase shares for cash on the open market, from time to time, in privately negotiated transactions or block transactions, or through an accelerated repurchase agreement. The timing of such repurchases is dependent on price, market conditions and applicable regulatory requirements. Upon repurchase of the shares, we reduced our common stock for the par value of the shares with the excess being applied against additional paid-in capital.

During the first quarter of 2011 we repurchased shares under this program with an aggregate value of \$2,497. Of this amount \$110 reduced common stock and \$2,387 reduced additional paid-in capital.

**Note 15: Impairment of Long-lived Asset**

On September 10, 2010 a fire at our Portugal manufacturing site caused significant damage to a portion of one building and production in that specific unit was temporarily idled. The portion of the building that was damaged produced water-based polymers used to manufacture both adhesive and resin products. During the first quarter of 2011, a decision was made to discontinue production of the polymers used in certain resin products that had been produced by our Portugal manufacturing site. As a result, we performed an impairment test on the Portugal trademarks and trade names used in resin products. In accordance with accounting standards, we calculated the fair value using a discounted cash flow approach. As a result of this analysis, we recorded an impairment charge of \$332 (\$220 after tax). The intangible assets are recorded in our EIMEA operating segment.

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations****Overview**

The Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) should be read in conjunction with the MD&A included in our Annual Report on Form 10-K for the year ended November 27, 2010 for important background information related to our business.

Net revenue in the first quarter of 2011 increased 9.7 percent over the first quarter of 2010. Organic sales growth, which we define as revenue growth due to changes in sales volume and selling prices, increased 9.0 percent as compared to the first quarter of 2010. The growth was broad-based across market segments and geography. Specifically, our EIMEA region continued its robust organic sales growth trend posting a 13.2 percent increase over prior year. Our Asia Pacific region posted a net revenue increase of over 30 percent. Raw material costs continued to increase in the first quarter of 2011 primarily due to supply shortages and higher cost of feedstocks. This contributed to a decline in gross margin in the first quarter of 2011 to 28.5 percent from 31.6 percent in the first quarter of 2010. Finally, we reduced our SG&A expenses as a percentage of revenue by 80 basis points in the first quarter relative to last year's first quarter.

Net income attributable to H.B. Fuller for the first quarter of 2011 was \$14.4 million as compared to \$19.0 million in the first quarter of 2010. On a diluted earnings per share basis, the first quarter of 2011 was \$0.29 per share as compared to \$0.38 per share for the same period last year.

**Results of Operations****Net revenue:**

| (\$ in millions) | February 26,<br>2011 | 13 Weeks Ended<br>February 27,<br>2010 | 2011 vs<br>2010 |
|------------------|----------------------|--|-----------------|
| Net revenue      | \$ 339.5             | \$ 309.4                               | 9.7%            |

We review variances in net revenue in terms of changes related to product pricing, sales volume, changes in foreign currency exchange rates and acquisitions. The following table shows the net revenue variance analysis for the first quarter of 2011 compared to the same period in 2010:

|                 | 13 Weeks<br>Ended<br>February 26, 2011 |
|-----------------|--|
| Product pricing | 6.8%                                   |
| Sales volume    | 2.2%                                   |
| Currency        | (1.0%)                                 |
| Acquisitions    | 1.7%                                   |
|                 | 9.7%                                   |

Organic sales growth was a positive 9.0 percent (positive 6.8 percent from product pricing and positive 2.2 percent from sales volume) in the first quarter of 2011 as compared to the same period last year. The organic growth was driven by double-digit growth in both the EIMEA and Asia Pacific operating segments. The negative currency effects in the quarter were primarily the result of the weakening of the Euro partially offset by the strengthening of the Australian dollar as compared to the U.S. The 1.7 percent net revenue increase from acquisitions in 2011 was due to the acquisition of Revertex Finewaters, early in the third quarter of 2010.

**Cost of sales:**

| (\$ in millions) | February 26,<br>2011 | 13 Weeks Ended<br>February 27,<br>2010 | 2011 vs<br>2010 |
|------------------|----------------------|--|-----------------|
|------------------|----------------------|--|-----------------|

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|                        |          |    |       |       |
|------------------------|----------|----|-------|-------|
| Cost of sales:         | \$ 242.6 | \$ | 211.8 | 14.6% |
| Percent of net revenue | 71.5%    |    | 68.4% |       |

The 14.6 percent increase in the cost of sales in the first quarter of 2011 as compared to the first quarter of 2010 was driven by the increases in raw material costs primarily due to supply shortages and higher cost of feedstocks. Each of our four operating segments was impacted by the rising raw material costs. The shortages were driven by refineries reducing the supply of the by-products that are used as raw materials in the production of adhesives and increased demand in adjacent industries.

**Gross profit:**

| (\$ in millions)       | February 26,<br>2011 | 13 Weeks Ended<br>February 27,<br>2010 | 2011 vs<br>2010 |
|------------------------|----------------------|--|-----------------|
| Gross profit           | \$ 96.9              | \$ 97.7                                | (0.8%)          |
| Percent of net revenue | 28.5%                | 31.6%                                  |                 |

The lower gross profit margin for the first quarter of 2011 as compared to the same period in 2010 resulted from the increase in raw material costs which more than offset the benefits from the increased net revenue.

**Selling, general and administrative (SG&A) expenses:**

| (\$ in millions)       | February 26,<br>2011 | 13 Weeks Ended<br>February 27,<br>2010 | 2011 vs<br>2010 |
|------------------------|----------------------|--|-----------------|
| SG&A                   | \$ 75.7              | \$ 71.4                                | 5.9%            |
| Percent of net revenue | 22.3%                | 23.1%                                  |                 |

SG&A expenses increased \$4.2 million or 5.9 percent from the first quarter of 2010. The increases were largely due to higher costs associated with adding resources to our sales and technical organizations. We continue to invest in growth despite the sluggish economic environment. We reduced our SG&A expenses as a percentage of revenue by 80 basis points in the first quarter relative to last year's first quarter.

**Asset impairment charges:**

| (\$ in millions)         | February 26,<br>2011 | 13 Weeks Ended<br>February 27,<br>2010 | 2011 vs<br>2010 |
|--------------------------|----------------------|--|-----------------|
| Asset impairment charges | \$ 0.3               | \$                                     | NMP             |

NMP = Non-meaningful percentage

In the fourth quarter of 2010, a fire at our Portugal manufacturing site caused production to be temporarily idled. During the first quarter of 2011, a decision was made to discontinue production of the polymer used in certain resin products that had been produced by our Portugal manufacturing site. Asset impairment charges of \$0.3 million relate to the impairment of trademarks and trade names used in the abandoned resin products.

**Other income (expense), net:**

| (\$ in millions)            | February 26,<br>2011 | 13 Weeks Ended<br>February 27,<br>2010 | 2011 vs<br>2010 |
|-----------------------------|----------------------|--|-----------------|
| Other income (expense), net | \$ 0.3               | \$ (0.1)                               | NMP             |

NMP = Non-meaningful percentage

Interest income increased \$0.3 million in the first quarter of 2011 compared to the first quarter of 2010. Currency translation and re-measurement losses were \$0.3 million in the first quarter of 2011 as compared to gains of \$0.1 million in the first quarter of 2010.

**Interest expense:**

| (\$ in millions) | February 26,<br>2011 | 13 Weeks Ended<br>February 27,<br>2010 | 2011 vs<br>2010 |
|------------------|----------------------|--|-----------------|
| Interest expense | \$ 2.6               | \$ 1.9                                 | 32.5%           |

The higher interest expense in the first quarter of 2011 as compared to the first quarter of 2010 was due to a change in the mix of debt. The weighted average interest rate on debt held in the first quarter of 2011 was higher than the first quarter of 2010.

**Income taxes:**

| (\$ in millions)   | February 26,<br>2011 | 13 Weeks Ended<br>February 27,<br>2010 | 2011 vs<br>2010 |
|--------------------|----------------------|--|-----------------|
| Income taxes       | \$ 6.3               | \$ 7.1                                 | (11.0%)         |
| Effective tax rate | 33.7%                | 29.1%                                  |                 |

Income tax expense of \$6.3 million in the first quarter of 2011 includes \$0.6 million of discrete tax expense. Excluding these items, the overall effective tax rate was 30.5 percent. Excluding the \$1.1 million of discrete tax benefits in the first quarter of 2010, the overall effective tax rate was 33.8 percent. The primary reason for the lower rate in 2011 resulted from changes in the geographic mix of pretax earnings as compared to 2010.

**Income from equity method investments:**

| (\$ in millions)                      | February 26,<br>2011 | 13 Weeks Ended<br>February 27,<br>2010 | 2011 vs<br>2010 |
|---------------------------------------|----------------------|--|-----------------|
| Income from equity method investments | \$ 1.9               | \$ 1.8                                 | 2.5%            |

The income from equity method investments relates to our 50 percent ownership of the Sekisui-Fuller joint venture in Japan. The first quarter results reflected the higher net income recorded by the joint venture in 2011 compared to the same period of 2010 due mainly to stronger gross profit margins.

**Net (income) loss attributable to noncontrolling interests:**

| (\$ in millions)   | February 26,<br>2011 | 13 Weeks Ended<br>February 27,<br>2010 | 2011 vs<br>2010 |
|--|----------------------|--|-----------------|
| Net (income) loss attributable to noncontrolling interests | \$ 0.14              | \$ (0.02)                              | NMP             |

NMP = Non-meaningful percentage

Operating losses in our China entities led to a \$0.14 million net loss attributable to noncontrolling interests in the first quarter of 2011. This compared to a \$0.02 million net income attributable to noncontrolling interests in the first quarter of 2010.



**Net income attributable to H.B. Fuller:**

| (\$ in millions)                       | 13 Weeks Ended       |                      | 2011 vs<br>2010 |
|--|----------------------|----------------------|-----------------|
|  | February 26,<br>2011 | February 27,<br>2010 |                 |
| Net income attributable to H.B. Fuller | \$ 14.4              | \$ 19.0              | (24.3%)         |
| Percent of net revenue                 | 4.2%                 | 6.1%                 |                 |

The net income attributable to H.B. Fuller for the first quarter of 2011 was \$14.4 million compared to \$19.0 million for the first quarter of 2010. The diluted EPS for the first quarter of 2011 was \$0.29 per share as compared to \$0.38 per share for the first quarter of 2010. The continued increase in raw material costs and the increase in SG&A expenses more than offset the 9.7 percent increase in net revenue.

**Operating Segment Results**

Our operations are managed through the four primary geographic regions: North America, EIMEA (Europe, India, Middle East, Africa), Latin America and Asia Pacific.

The tables below provide certain information regarding the net revenue and operating income of each of our operating segments. For segment evaluation by the chief operating decision maker, operating income is defined as gross profit less SG&A expenses.

**Net Revenue by Segment:**

| (\$ in millions) | 13 Weeks Ended    |               |                   |               |
|------------------|-------------------|---------------|-------------------|---------------|
|                  | February 26, 2011 |               | February 27, 2010 |               |
|                  | Net<br>Revenue    | % of<br>Total | Net<br>Revenue    | % of<br>Total |
| North America    | \$ 134.9          | 40%           | \$ 127.1          | 41%           |
| EIMEA            | 100.8             | 30%           | 94.0              | 30%           |
| Latin America    | 59.9              | 17%           | 55.3              | 18%           |
| Asia Pacific     | 43.9              | 13%           | 33.0              | 11%           |
| <b>Total</b>     | <b>\$ 339.5</b>   | <b>100%</b>   | <b>\$ 309.4</b>   | <b>100%</b>   |

**Operating Income by Segment:**

| (\$ in millions) | 13 Weeks Ended      |               |                     |               |
|------------------|---------------------|---------------|---------------------|---------------|
|                  | February 26, 2011   |               | February 27, 2010   |               |
|                  | Operating<br>Income | % of<br>Total | Operating<br>Income | % of<br>Total |
| North America    | \$ 14.9             | 70%           | \$ 17.2             | 65%           |
| EIMEA            | 1.9                 | 9%            | 4.1                 | 16%           |
| Latin America    | 3.4                 | 16%           | 2.8                 | 11%           |
| Asia Pacific     | 1.1                 | 5%            | 2.1                 | 8%            |
| <b>Total</b>     | <b>\$ 21.3</b>      | <b>100%</b>   | <b>\$ 26.2</b>      | <b>100%</b>   |

The following table provides a reconciliation of operating income to income before income taxes and income from equity method investments, as reported on the Consolidated Statements of Income.

13 Weeks Ended

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| (\$ in millions)   | February 26,<br>2011 | February 27,<br>2010 |
|--|----------------------|----------------------|
| Operating income   | \$ 21.3              | \$ 26.2              |
| Asset impairment charges   | (0.3)                |                      |
| Other income (expense), net  | 0.2                  | (0.1)                |
| Interest expense   | (2.6)                | (1.9)                |
| <br>   |                      |                      |
| Income before income taxes and income from equity method investments | \$ 18.6              | \$ 24.2              |

**North America**

The following table shows the net revenue generated from the two reporting units of the North America operating segment.

| (\$ in millions)      | February 26,<br>2011 | 13 Weeks Ended<br>February 27,<br>2010 | 2011 vs<br>2010 |
|-----------------------|----------------------|--|-----------------|
| Adhesives             | \$ 108.0             | \$ 100.6                               | 7.5%            |
| Construction Products | 26.9                 | 26.5                                   | 1.3%            |
| <b>Total</b>          | <b>\$ 134.9</b>      | <b>\$ 127.1</b>                        | <b>6.2%</b>     |

The following tables provide details of North America net revenue variances by reporting units. The Pricing/Sales Volume variance is viewed as organic growth.

|                      | 13 Weeks Ended February 26, 2011 vs<br>February 27, 2010 |                          |             |
|----------------------|--|--------------------------|-------------|
|                      | Adhesives  | Construction<br>Products | Total       |
| Pricing/Sales Volume | 7.0%   | 1.3%                     | 5.9%        |
| Currency             | 0.5%   |                          | 0.3%        |
| <b>Total</b>         | <b>7.5%</b>  | <b>1.3%</b>              | <b>6.2%</b> |

The following table reflects the operating income by reporting unit of the North America operating segment.

| (\$ in millions)      | February 26,<br>2011 | 13 Weeks Ended<br>February 27,<br>2010 | 2011 vs<br>2010 |
|-----------------------|----------------------|--|-----------------|
| Adhesives             | \$ 15.2              | \$ 17.2                                | (11.6%)         |
| Construction Products | (0.3)                |  | NMP             |
| <b>Total</b>          | <b>\$ 14.9</b>       | <b>\$ 17.2</b>                         | <b>(13.5%)</b>  |

|                         |       |       |
|-------------------------|-------|-------|
| Segment profit margin % | 11.0% | 13.6% |
|-------------------------|-------|-------|

NMP = Non-meaningful percentage

Note: Individual reporting unit results are subject to numerous allocations of segment-wide costs that may or may not have been focused on that particular reporting unit for a particular reporting period. The costs of these allocated resources are not tracked on a where-used basis as financial performance is managed to maximize the total operating segment performance. Therefore, the above financial information should only be used for directional indications of performance.

**Total North America:** Net revenue increased 6.2 percent in the first quarter of 2011 compared to the first quarter of 2010. The increase was mainly due to a 5.8 percent increase in average selling prices. Year over year volume was relatively flat. As the economy continues its recovery, demand for raw materials has increased at the same time supply has been constrained. The result is a significant increase in raw material costs. Despite implementing selling price increases, we have not been able to completely offset the rising raw material costs, leading to a lower gross profit margin in the first quarter of 2011 compared to the first quarter of 2010. SG&A expenses were up over prior

year as we continued to invest in our commercial organization. Operating income declined 13.5 percent in the first quarter of 2011 compared to prior year as a result of the decrease in gross profit margin combined with higher SG&A expenses.

**Adhesives:** Raw material prices continued to increase as the global demand for feedstocks that are the basis of many of our adhesives raw materials has continued to increase. The 7.5 percent increase in net revenue over prior year was mainly attributable to an increase in average selling prices as year over year sales volume was flat. The gross profit margin declined compared to prior year as selling price increases were not enough to offset the increase in raw material costs. The impact of increasing raw material costs combined with higher SG&A expenses resulted in the 11.6 percent decline in operating income in the first quarter of 2011 compared to the first quarter of 2010.

**Construction Products:** Housing construction continues to lag which is reflected in the relatively flat performance in the first quarter of 2011. Both average selling prices and sales volumes were up slightly compared to prior year. The 1.3 percent increase in net revenue over prior year was due to positive results in our distribution business offset by a decrease in our retail business. Gross profit margins decreased slightly related to a minor increase in raw material costs. A reorganization in our sales and marketing area contributed to an increase in SG&A expense. The reorganization is intended to support marketing initiatives and promote growth. The operating loss in the first quarter of 2011 is the result of reduced gross profit generation and the increase in SG&A expense.

## EIMEA

| (\$ in millions)       | 13 Weeks Ended       |                      | 2011 vs<br>2010 |
|------------------------|----------------------|----------------------|-----------------|
|                        | February 26,<br>2011 | February 27,<br>2010 |                 |
| Net Revenue            | \$ 100.8             | \$ 94.0              | 7.2%            |
| Operating Income       | \$ 1.9               | \$ 4.1               | (52.6%)         |
| Segment profit margin% | 1.9%                 | 4.4%                 |                 |

The following table provides details of the EIMEA net revenue variances. The Pricing/Sales Volume variance is viewed as organic growth.

| 13 Weeks Ended February 26, 2011<br>vs February 27, 2010 |             |
|--|-------------|
| Pricing/Sales Volume                                     | 13.2%       |
| Currency   | (6.0%)      |
| <b>Total</b>   | <b>7.2%</b> |

**Total EIMEA:** The organic sales growth increased 13.2 percent in the first quarter of 2011 compared to the first quarter of 2010. The increase resulted from both selling price increases and improved sales volume. Investments made in the sales organization continue to have positive effects on organic sales growth. The effects of the weaker Euro resulted in a 6.0 percent decrease in net revenue. The 2010 net revenue included the polysulfide-based insulating glass product line which we exited in the second quarter of 2010. The gross profit margin decreased in the first quarter of 2011 compared to the first quarter of 2010 as shortages in certain raw materials and rapid raw material cost increases exceeded the increase in organic sales growth. The political unrest in North Africa, primarily Egypt and Libya, and the resulting production interruptions, also contributed to the lower gross profit margin as we incurred additional costs to supply our customers. The SG&A expenses increased mainly due to the investments in the sales organization. The combination of the lower gross profit margin and the increase in SG&A expenses led to a 52.6 percent decline in operating income in the first quarter of 2011 as compared to the same period last year.

## Latin America

The following table shows the net revenue generated from the two reporting units of the Latin America operating segment.

| (\$ in millions) | 13 Weeks Ended       |                      | 2011 vs<br>2010 |
|------------------|----------------------|----------------------|-----------------|
|                  | February 26,<br>2011 | February 27,<br>2010 |                 |
| Adhesives        | \$ 31.1              | \$ 29.1              | 6.9%            |

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|                     |         |         |       |
|---------------------|---------|---------|-------|
| Paints              | 28.8    | 26.2    | 10.0% |
| Total Latin America | \$ 59.9 | \$ 55.3 | 8.3%  |

The following table provides details of Latin America net revenue variances by reporting units. The Pricing/Sales Volume variance is viewed as organic growth.

|                      | 13 Weeks Ended February 26, 2011 vs<br>February 27, 2010 |        |       |
|----------------------|--|--------|-------|
|                      | Adhesives  | Paints | Total |
| Pricing/Sales Volume | 6.9%   | 10.0%  | 8.3%  |

The following table reflects the operating income (loss) by reporting unit of the Latin America operating segment.

| (\$ in millions)           | 13 Weeks Ended       |                      |                 |
|----------------------------|----------------------|----------------------|-----------------|
|                            | February 26,<br>2011 | February 27,<br>2010 | 2011 vs<br>2010 |
| Adhesives                  | \$ 1.0               | \$ 1.9               | (50.3%)         |
| Paints                     | 2.4                  | 0.9                  | 167.6%          |
| <b>Total Latin America</b> | <b>\$ 3.4</b>        | <b>\$ 2.8</b>        | <b>17.7%</b>    |
| Segment profit margin %    | 5.6%                 | 5.0%                 |                 |

Note: Individual reporting unit results are subject to numerous allocations of segment-wide costs that may or may not have been focused on that particular reporting unit for a particular reporting period. The costs of these allocated resources are not tracked on a where-used basis as financial performance is managed to maximize the total operating segment performance. Therefore, the above financial information should only be used for directional indications of performance.

**Total Latin America:** Both reporting units had positive net revenue growth in the first quarter of 2011 as compared to the first quarter of 2010. Increases in average selling prices were partially offset by a decrease in sales volume. Raw material cost increases and supply shortages had a negative impact on both reporting units during the quarter. The increase in the Paints gross profit margin was the main driver for the increase in operating income during the quarter as compared to the same quarter of 2010.

**Adhesives:** The net revenue growth experienced in 2011 can be attributed to increased average selling price partially offset by a decline in sales volume. The gross profit margin decreased in the first quarter of 2011 compared to the first quarter of 2010 due to the significant increase in raw material costs. SG&A expenses increased from last year at virtually the same pace as the growth in net revenue. The lower gross profit margin was the key factor in the 50.3 percent decline in operating income in the first quarter of 2011 as compared to last year.

**Paints:** The 10.0 percent net revenue increase experienced in the first quarter of 2011 as compared to the first quarter of 2010 was mainly due to increases in average selling price and by better economic conditions in Central America. The gross profit margin increased over last year due to the favorable mix of sales as well as the impact from selling price increases. The favorable mix of sales was due to our strategy to focus on higher-end products versus the lower-end commodity products. The improved gross profit margin in 2011 was the main driver of improved operating income for the quarter as compared to the same period in 2010.

#### Asia Pacific

| (\$ in millions)        | 13 Weeks Ended       |                      |                 |
|-------------------------|----------------------|----------------------|-----------------|
|                         | February 26,<br>2011 | February 27,<br>2010 | 2011 vs<br>2010 |
| Net Revenue             | \$ 43.9              | \$ 33.0              | 32.8%           |
| Operating Income        | \$ 1.1               | \$ 2.1               | (48.4%)         |
| Segment profit margin % | 2.4%                 | 6.2%                 |                 |

The following table provides details of Asia Pacific net revenue. The Pricing/Sales Volume variance is viewed as organic growth.

|                         | <b>13 Weeks Ended February 26, 2011<br/>vs February 27, 2010</b> |
|-------------------------|--|
| Pricing/Sales Volume    | 10.0%  |
| Currency                | 6.6%   |
| Acquisition/Divestiture | 16.2%  |
| Total                   | 32.8%  |

**Total Asia Pacific:** Net revenue increased 32.8 percent compared to prior year due to organic sales growth of 10% and the Revertex Finewaters acquisition in Malaysia which added \$5.4 million or 16.2 percent. The organic sales growth is made up of a 7.3 percent increase in sales volume and a 2.7 percent increase in average selling prices compared to prior year. The growth is the result of the expansion and investments we have been making in this operating segment. Also contributing to the increase in revenue were positive currency effects of 6.6 percent or \$2.2 million. The currency effect was largely driven by the strengthening of the Australian dollar as compared to the U.S. dollar. SG&A expenses increased significantly compared to prior year as a result of the acquisition and our investments in sales and marketing. Increases in raw material prices and the impact of the acquisition and currency effects resulted in a decrease in gross profit margin despite the organic growth. The reduced gross profit generation combined with the increases in SG&A expenses led to the 48.4 percent reduction in operating income in the first quarter of 2011 as compared to the first quarter of 2010.

#### Financial Condition, Liquidity and Capital Resources

Total cash and cash equivalents as of February 26, 2011 were \$121.9 million as compared to \$133.3 million as of November 27, 2010 and \$149.0 million as of February 27, 2010. Total long and short-term debt was \$239.2 million as of February 26, 2011, \$250.7 million as of November 27, 2010 and \$279.2 million as of February 27, 2010. The total debt to total capital ratio as measured by Total Debt divided by (Total Debt plus Total Equity) was 26.4 percent as of February 26, 2011 as compared to 28.3 percent as of November 27, 2010 and 32.2 percent as of February 27, 2010. The lower ratio as of February 26, 2011 compared to November 27, 2010 and February 27, 2010 was due to higher equity from net earnings and lower quarter-end debt levels.

We believe that cash flows from operating activities will be adequate to meet our ongoing liquidity and capital expenditure needs. In addition, we believe we have the ability to obtain both short-term and long-term debt to meet our financing needs for the foreseeable future.

Our credit agreements include restrictive covenants that, if not met, could lead to a renegotiation of our credit lines and a significant increase in our cost of financing. At February 26, 2011, we were in compliance with all covenants of our contractual obligations as shown in the following table:

| (\$ in millions)                  |                                       |                      |  | <b>Result as of<br/>February 26,<br/>2011</b> |
|-----------------------------------|---------------------------------------|----------------------|--|---|
| <b>Covenant</b>                   | <b>Debt Instrument</b>                | <b>Measurement</b>   |  |   |
| TTM EBITDA / TTM Interest Expense | Revolving Credit Facility & Term Loan | Not less than 2.5    |  | 13.7  |
| Total Indebtedness / TTM EBITDA   | Revolving Credit Facility & Term Loan | Not greater than 3.5 |  | 1.6   |
| TTM EBITDA / TTM Interest Expense | Private Placement                     | Not less than 2.5    |  | 12.9  |
| Total Indebtedness / TTM EBITDA   | Private Placement                     | Not greater than 3.5 |  | 1.7   |

TTM = Trailing 12 months

For the revolving credit facility and term loan, EBITDA is defined as income from continuing operations plus goodwill and other impairment charges plus interest expense plus income tax expense plus depreciation and amortization expense.

For the 2010 private placement, EBITDA is defined as income from continuing operations plus interest expense plus income tax expense plus depreciation and amortization expense.

We believe we have the ability to meet all of our contractual obligations and commitments in fiscal 2011. Included in these obligations are the following scheduled debt payments:

\$5.6 million payments on term loan, due March 31, June 30, and September 30, 2011, are expected to be paid using existing cash.

#### Selected Metrics of Liquidity

Key metrics we monitor are net working capital as a percent of annualized net revenue, trade account receivable days sales outstanding (DSO), inventory days on hand, free cash flow and debt capitalization ratio.

|  | February 26,<br>2011 | February 27,<br>2010 |
|--|----------------------|----------------------|
| Net working capital as a percentage of annualized net revenue <sup>1</sup> | 18.2%                | 17.3%                |
| Accounts receivable DSO <sup>2</sup>                                       | 57 Days              | 50 Days              |
| Inventory days on hand <sup>3</sup>  | 52 Days              | 55 Days              |
| Free cash flow <sup>4</sup>  | (\$7.9) million      | (\$11.6) million     |
| Total debt to total capital ratio <sup>5</sup>                             | 26.4%                | 32.2%                |

<sup>1</sup> Current quarter net working capital (trade receivables, net of allowance for doubtful accounts plus inventory minus trade payables) divided by annualized net revenue (current quarter multiplied by four).

<sup>2</sup> (Trade receivables less the allowance for doubtful accounts at the balance sheet date) multiplied by 56 (8 weeks) and divided by the net revenue for the last 2 months of the quarter.

<sup>3</sup> Total inventory multiplied by 56 and divided by cost of sales (excluding delivery costs) for the last 2 months of the quarter.

<sup>4</sup> Net cash provided by operations from continuing operations, less purchased property, plant and equipment and dividends paid.

<sup>5</sup> Total debt divided by (total debt plus total stockholders' equity).

Another key metric is the return on gross investment, or ROGI. The calculation is represented by gross cash flow divided by Gross Investment.

Gross cash flow is defined as: gross profit, less SG&A less taxes at a non-GAAP standard rate of 29 percent, plus depreciation and amortization expenses, less maintenance capital expenditures, a non-GAAP financial measure defined as 50 percent of total depreciation expense. Gross cash flow is calculated using trailing 12 month information.

Gross investment is defined as total assets plus accumulated depreciation less non-debt current liabilities less cash.

ROGI was introduced because we believe it provides a true measure of return on investment, it is a better way to internally measure performance and it is focused on the long term. The ROGI calculated at February 26, 2011 and November 27, 2010 were 6.8 percent and 7.3 percent, respectively.



The following table shows the ROGI calculation based on the definition above compared to a calculation using all GAAP-based data. We believe the use of certain non-GAAP financial measures provides a better calculation of ROGI because they eliminate fluctuations not specifically related to the return on the current investment base.

| (\$ in millions)  | Trailing 12 months<br>as of February 26, 2011 |                                     |
|---|---|-------------------------------------|
|   | ROGI<br>(Management<br>calculation)           | ROGI<br>(GAAP-based<br>calculation) |
| Gross profit <sup>1</sup>                                 | \$ 398.2                                      | \$ 396.4                            |
| Selling, general and administrative expenses <sup>2</sup> | (296.3)                                       | (297.1)                             |
| Operating income  | 101.9   | 99.3                                |
| Taxes <sup>3</sup>  | (29.6)  | (30.6)                              |
| Depreciation and amortization                             | 40.8  | 40.8                                |
| Maintenance capital expenditures <sup>4</sup>             | (15.2)  | (32.6)                              |
| Gross cash flow   | \$ 97.9                                       | \$ 76.9                             |
| Gross investment  | \$ 1,436.7                                    | \$ 1,436.7                          |
| Return on gross investment                                | 6.8%  | 5.4%                                |

<sup>1</sup> The ROGI (management calculation) gross profit excludes exit costs and asset impairment charges of \$1.8 associated with exiting the polysulfide insulating glass product line in Europe.

<sup>2</sup> The ROGI (management calculation) selling, general and administrative expenses excludes exit costs of \$0.8 associated with exiting the polysulfide insulating glass product line in Europe.

<sup>3</sup> The ROGI calculation for management measurement purposes uses a tax rate of 29 percent. The GAAP rate is based on actual tax expense including any discrete items.

<sup>4</sup> Maintenance capital expenditures used for the management calculation of ROGI is 50 percent of total depreciation expense whereas the GAAP-based amount is the actual capital expenditures from the cash flow statement.

#### Summary of Cash Flows

#### Cash Flows from Operating Activities:

| (\$ in millions)                          | 13 Weeks Ended       |                      |
|---|----------------------|----------------------|
|   | February 26,<br>2011 | February 27,<br>2010 |
| Net cash provided by operating activities | \$ 1.5               | \$ 1.1               |

Net income attributable to H.B. Fuller plus depreciation and amortization expense totaled \$24.3 million in the first quarter of 2011 as compared to \$29.4 million in the first quarter of 2010. Changes in net working capital (trade receivables, inventory and trade payables) accounted for a use of cash of \$3.3 million in the first three months of 2011 as compared to a use of cash of \$7.5 million in the first three months of 2010.

The table below shows the cash flow impact due to changes in the components of net working capital:

| (\$ in millions)       | 13 Weeks Ended       |                      |
|------------------------|----------------------|----------------------|
|                        | February 26,<br>2011 | February 27,<br>2010 |
| Trade receivables, net | \$ (2.5)             | \$ 13.4              |
| Inventory              | (20.1)               | (18.9)               |
| Trade payables         | 19.3                 | (2.0)                |
| Total cash flow impact | \$ (3.3)             | \$ (7.5)             |



**Trade Receivables, net** The higher sales activity and higher DSO in the first quarter of 2011 was the primary reason for the use of cash of \$2.5 million compared to a source of cash of \$13.4 million in 2010. The DSO was 57 days at February 26, 2011 and 50 days at February 27, 2010. The increase in DSO was driven by increases in the EIMEA, Latin America and Asia Pacific operating segments.

**Inventory** The use of cash in 2011 was directly related to the increase in sales volume, higher raw material costs and the purchases of inventory based on availability instead of forecasted usage. Certain raw materials have been in short supply so purchases have been made based on availability instead of forecasted usage. This resulted in some balances being higher than normal as of February 26, 2011. The downward management of our inventory in the fourth quarter of 2010 also impacted our use of cash in the current quarter. Inventory days on hand were 52 days as of February 26, 2011 as compared to 55 days as of February 27, 2010. All operating segments with the exception of EIMEA reported lower days on hand at the end of the first quarter of 2011 as compared to the end of the first quarter of 2010.

**Trade Payables** The large source of cash in the first three months of 2011 was primarily due to the increase in inventory and the timing of payments.

#### **Cash Flows from Investing Activities:**

| (\$ in millions)                      | 13 Weeks Ended       |                      |
|---------------------------------------|----------------------|----------------------|
|                                       | February 26,<br>2011 | February 27,<br>2010 |
| Net cash used in investing activities | \$ (6.0)             | \$ (9.2)             |

Purchases of property, plant and equipment were \$6.1 million in the first quarter of 2011 as compared to \$9.4 million for the same period of 2010. Construction of the manufacturing plant in Nanjing, China accounted for \$3.2 million of the increased spending in 2010 as compared to this year. We do not anticipate significant repair and maintenance activities on existing property, plant and equipment as a result of current or past capital spending policies.

#### **Cash Flows from Financing Activities:**

| (\$ in millions)                                    | 13 Weeks Ended       |                      |
|---|----------------------|----------------------|
|   | February 26,<br>2011 | February 27,<br>2010 |
| Net cash provided by (used in) financing activities | \$ (10.9)            | \$ 63.5              |

Proceeds of long-term debt were \$33.0 million in the first quarter of 2011 compared to \$273.0 million for the first quarter of 2010. Included in the 2010 proceeds of long-term debt was our note purchase agreement under which we issued \$150.0 million in aggregate principal amount of senior unsecured notes. Repayments of long-term debt were \$38.6 million in the first quarter of 2011 compared to \$211.0 million for the same period of 2010. The 2010 repayment of long-term debt was primarily to pay down the revolving credit that had been used to fund pension contributions in the fourth quarter of 2009. Cash generated from the exercise of stock options was \$4.8 million and \$1.2 million for the first quarter of 2011 and 2010, respectively. The higher 2011 cash generated from the exercise of stock options was mainly due to exercises by the former CEO as his departure required the exercise of certain stock option awards prior to the end of the first quarter. Repurchases of common stock were \$3.1 million in the first quarter of 2011 compared to \$0.4 million in the same period of 2010. The higher 2011 repurchases of common stock was due to \$2.5 million from our September 30, 2010 share repurchase program.

#### **Forward-Looking Statements and Risk Factors**

The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. In this Quarterly Report on Form 10-Q, we discuss expectations regarding our future performance which include anticipated financial performance, savings from restructuring and process initiatives, global economic conditions,

liquidity requirements, the impact of litigation and environmental matters, the effect of new accounting pronouncements and one-time accounting charges and credits, and similar matters. This Quarterly Report on Form 10-Q contains forward looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements may be identified by the use of words like plan, expect, aim, believe, project, anticipate, intend, estimate, will, should, could (including the negative or variations thereof) and other expressions of future events and trends. These plans and expectations are based upon certain underlying assumptions, including those mentioned with the specific statements. Such assumptions are in turn based upon internal estimates and analyses of current market conditions and trends, our plans and strategies, economic conditions and other factors. These plans and expectations and the assumptions underlying them are necessarily subject to risks and uncertainties inherent in projecting future conditions and results. Actual results could differ materially from expectations expressed in the forward-looking statements if one or more of the underlying assumptions and expectations proves to be inaccurate or is unrealized. In addition to the factors described in this report, Part II, Item 1A. Risk Factors in this report and Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the fiscal year ended November 27, 2010, identify some of the important factors that could cause our actual results to differ materially from those in any such forward-looking statements. This list of important factors does not include all such factors nor necessarily present them in order of importance. In order to comply with the terms of the safe harbor, we have identified these important factors which could affect our financial performance and could cause our actual results for future periods to differ materially from the anticipated results or other expectations expressed in the forward-looking statements. Additionally, the variety of products sold by us and the regions where we do business makes it difficult to determine with certainty the increases or decreases in revenues resulting from changes in the volume of products sold, currency impact, changes in geographic and product mix and selling prices. Our best estimates of these changes as well as changes in other factors have been included. References to volume changes include volume, product mix and delivery charges, combined. These factors should be considered, together with any similar risk factors or other cautionary language, which may be made elsewhere in this Quarterly Report on Form 10-Q.

We may refer to Part II, Item 1A. Risk Factors and this section of the Form 10-Q to identify risk factors related to other forward looking statements made in oral presentations, including investor conferences and/or webcasts open to the public.

This disclosure, including that under Forward-Looking Statements and Risk Factors, and other forward-looking statements and related disclosures made by us in this report and elsewhere from time to time, represents our best judgment as of the date the information is given. We do not undertake responsibility for updating any of such information, whether as a result of new information, future events, or otherwise, except as required by law. Investors are advised, however, to consult any further public company disclosures (such as in filings with the Securities and Exchange Commission or in company press releases) on related subjects.

### **Item 3. Quantitative and Qualitative Disclosures about Market Risk**

**Market Risk:** We are exposed to various market risks, including changes in interest rates, foreign currency rates and prices of raw materials. Market risk is the potential loss arising from adverse changes in market rates and prices, such as interest rates, foreign currency exchange rates and cost of raw materials.

Our financial performance has been, and may continue to be, negatively affected by the unfavorable economic conditions. Continued or further recessionary economic conditions may have an adverse impact on our sales volumes, pricing levels and profitability. As domestic and international economic conditions change, trends in discretionary consumer spending also become unpredictable and subject to reductions due to uncertainties about the future. A general reduction in consumer discretionary spending due to recession in the domestic and international economies, or uncertainties regarding future economic prospects, could have a material adverse effect on our results of operations.

**Interest Rate Risk:** Exposure to changes in interest rates result primarily from borrowing activities used to fund operations. Committed floating rate credit facilities are used to fund a portion of operations. We believe that probable near-term changes in interest rates would not materially affect financial condition, results of operations or cash flows. The annual impact on interest expense of a one-percentage point interest rate change on the outstanding balance of our variable rate debt as of February 26, 2011 would be approximately \$1.6 million.

**Foreign Exchange Risk:** As a result of being a global enterprise, there is exposure to market risks from changes in foreign currency exchange rates, which may adversely affect operating results and financial condition. Approximately 61 percent of net revenue was generated outside of the United States for the first three months of

2011. Principal foreign currency exposures relate to the Euro, Canadian dollar, Australian dollar, British pound sterling, Japanese yen, Swiss franc, Argentine peso, Brazilian real, Chilean peso, Columbian peso, Costa Rican colon, Chinese renminbi, Honduran lempira, Indian rupee and Malaysian ringgit.

Our objective is to balance, where possible, local currency denominated assets to local currency denominated liabilities to have a natural hedge and minimize foreign exchange impacts. We enter into cross border transactions through importing and exporting goods to and from different countries and locations. These transactions generate foreign exchange risk as they create assets, liabilities and cash flows in currencies other than the local currency. This also applies to services provided and other cross border agreements among subsidiaries.

We take steps to minimize risks from foreign currency exchange rate fluctuations through normal operating and financing activities and, when deemed appropriate, through the use of derivative instruments. We do not enter into any speculative positions with regard to derivative instruments.

From a sensitivity analysis viewpoint, based on the financial results of the first three months of 2011, and foreign currency balance sheet positions as of February 26, 2011, a hypothetical overall 10 percent change in the U.S. dollar would have resulted in a change in net income attributable to H.B. Fuller of approximately \$0.6 million or \$0.01 per diluted share.

**Raw Materials:** The principal raw materials used to manufacture products include resins, polymers, synthetic rubbers, vinyl acetate monomer and plasticizers. We generally avoid sole source supplier arrangements for raw materials. While alternate supplies of most key raw materials are available, unplanned supplier production outages may lead to strained supply-demand situations for several key raw materials such as ethylene and propylene, several polymers and other petroleum derivatives such as waxes.

For the three months ended February 26, 2011, our single largest expenditure was the purchase of raw materials. Our objective is to purchase raw materials that meet both our quality standards and production needs at the lowest total cost. Most raw materials are purchased on the open market or under contracts that limit the frequency but not the magnitude of price increases. In some cases, however, the risk of raw material price changes is managed by strategic sourcing agreements which limit price increases to increases in supplier feedstock costs, while requiring decreases as feedstock costs decline. The leverage of having substitute raw materials approved for use wherever possible is used to minimize the impact of possible price increases.

#### **Item 4. Controls and Procedures**

##### **(a) Controls and procedures**

As of the end of the period covered by this report, we conducted an evaluation, under the supervision and with the participation of our president and chief executive officer and senior vice president, chief financial officer, of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934). Based on this evaluation, the president and chief executive officer and the senior vice president, chief financial officer concluded that, as of February 26, 2011, our disclosure controls and procedures were effective to ensure that information required to be disclosed by us in reports that we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms and to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934 is accumulated and communicated to us, including our principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

##### **(b) Change in internal control over financial reporting**

There were no changes in our internal control over financial reporting during our most recently completed fiscal quarter that have materially affected or are reasonably likely to materially affect our internal control over financial reporting, as defined in Rule 13a-15(f) under the Exchange Act.

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**PART II. OTHER INFORMATION****Item 1. Legal Proceedings**

**Environmental Matters.** From time to time, we are identified as a potentially responsible party (PRP) under the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) and/or similar state laws that impose liability for costs relating to the clean up of contamination resulting from past spills, disposal or other release of hazardous substances. We are also subject to similar laws in some of the countries where current and former facilities are located. Our environmental, health and safety department monitors compliance with applicable laws on a global basis.

Currently we are involved in various environmental investigations, clean up activities and administrative proceedings and lawsuits. In particular, we are currently deemed a PRP in conjunction with numerous other parties, in a number of government enforcement actions associated with hazardous waste sites. As a PRP, we may be required to pay a share of the costs of investigation and clean up of these sites. In addition, we are engaged in environmental remediation and monitoring efforts at a number of current and former operating facilities, including remediation of environmental contamination at the Sorocaba, Brazil facility. Soil and water samples were collected on and around the Sorocaba facility, and test results indicated that certain contaminants, including carbon tetrachloride and other solvents, exist in the soil at the Sorocaba facility and in the groundwater at both the Sorocaba facility and some neighboring properties. We are continuing to work with Brazilian regulatory authorities to implement and operate a remediation system at the site. As of February 26, 2011, \$1.1 million was recorded as a liability for expected remediation expenses remaining for this site. Depending on the results of the testing of our current remediation actions, we may be required to record additional liabilities related to remediation costs at the Sorocaba facility.

From time to time, we become aware of compliance matters relating to, or receive notices from, federal, state or local entities regarding possible or alleged violations of environmental, health or safety laws and regulations. We review the circumstances of each individual site, considering the number of parties involved, the level of potential liability or contribution of us relative to the other parties, the nature and magnitude of the hazardous substances involved, the method and extent of remediation, the estimated legal and consulting expense with respect to each site and the time period over which any costs would likely be incurred. To the extent we can reasonably estimate the amount of our probable liabilities for environmental matters, we establish a financial provision. As of February 26, 2011, we had reserved \$2.6 million, which represents our best estimate of probable liabilities with respect to environmental matters, inclusive of the accrual related to the Sorocaba facility as described above. However, the full extent of our future liability for environmental matters is difficult to predict because of uncertainty as to the cost of investigation and clean up of the sites, our responsibility for such hazardous substances and the number of and financial condition of other potentially responsible parties.

While uncertainties exist with respect to the amounts and timing of the ultimate environmental liabilities, based on currently available information, we do not believe that these matters, individually or in aggregate, will have a material adverse effect on our long-term financial condition. However, adverse developments and/or periodic settlements could negatively impact the results of operations or cash flows in one or more future periods.

**Other Legal Proceedings.** From time to time and in the ordinary course of business, we are a party to, or a target of, lawsuits, claims, investigations and proceedings, including product liability, personal injury, contract, patent and intellectual property, health and safety and employment matters. While we are unable to predict the outcome of these matters, we do not believe, based upon currently available information, that the ultimate resolution of any pending matter, individually or in aggregate, including the asbestos litigation described in the following paragraphs, will have a material adverse effect on our long-term financial condition. However, adverse developments and/or periodic settlements could negatively impact the results of operations or cash flows in one or more future periods.

We have been named as a defendant in lawsuits in which plaintiffs have alleged injury due to products containing asbestos manufactured more than 25 years ago. The plaintiffs generally bring these lawsuits against multiple defendants and seek damages (both actual and punitive) in very large amounts. In many cases, plaintiffs are unable to demonstrate that they have suffered any compensable injuries or that the injuries suffered were the result of exposure to products manufactured by us. We are typically dismissed as a defendant in such cases without payment. If the plaintiff presents evidence indicating that compensable injury occurred as a result of exposure to our products, the case is generally settled for an amount that reflects the seriousness of the injury, the length, intensity and character of exposure to products containing asbestos, the number and solvency of other defendants in the case, and the jurisdiction in which the case has been brought.

A significant portion of the defense costs and settlements in asbestos-related litigation continues to be paid by third parties, including indemnification pursuant to the provisions of a 1976 agreement under which we acquired a business from a third party. Historically, this third party routinely defended all cases tendered to it and paid

settlement amounts resulting from those cases. In the 1990s, the third party sporadically reserved its rights, but continued to defend and settle all asbestos-related claims tendered to it by us. In 2002, the third party rejected the tender of certain cases and indicated it would seek contributions for past defense costs, settlements and judgments. However, this third party is defending and paying settlement amounts, under a reservation of rights, in most of the asbestos cases tendered to the third party. As discussed below, during the fourth quarter of 2007, we and a group of other defendants, including the third party obligated to indemnify us against certain asbestos-related claims, entered into negotiations with certain law firms to settle a number of asbestos-related lawsuits and claims.

In addition to the indemnification arrangements with third parties, we have insurance policies that generally provide coverage for asbestos liabilities (including defense costs). Historically, insurers have paid a significant portion of our defense costs and settlements in asbestos-related litigation. However, certain of our insurers are insolvent. We have entered into cost-sharing agreements with our insurers that provide for the allocation of defense costs and, in some cases, settlements and judgments, in asbestos-related lawsuits. Under these agreements, we are required in some cases to fund a share of settlements and judgments allocable to years in which the responsible insurer is insolvent. In addition, to delineate our rights under certain insurance policies, in October 2009, we commenced a declaratory judgment action against one of our insurers in the United States District Court for the District of Minnesota. Additional insurers have been brought into the action to address issues related to the scope of their coverage. The lawsuit is in its early stages.

As referenced above, during the fourth quarter of 2007, we and a group of other defendants entered into negotiations with certain law firms to settle a number of asbestos-related lawsuits and claims over a period of years. In total, we had expected to contribute up to \$4.1 million, based on a present value calculation, towards the settlement amounts to be paid to the claimants in exchange for full releases of claims. Of this amount, our insurers had committed to pay \$2.0 million based on the probable liability of \$4.1 million. Our contributions toward settlements from the time of the agreement through the end of fiscal year 2010 were \$1.7 million with insurers paying \$0.9 million of that amount. Based on this experience we reduced our reserves in the fourth quarter of 2010 to an undiscounted amount of \$0.8 million with insurers expected to pay \$0.5 million. During the first quarter of 2011 we contributed another \$0.2 million toward settlements with insurers contributing \$0.1 million of that amount. This reduced our reserves for this agreement to \$0.6 million with an insurance receivable of \$0.4 million. These amounts represent our best estimate for the settlement amounts yet to be paid related to this agreement. Our reserve is recorded on an undiscounted basis.

In addition to the group settlement referenced above, a summary of the number of and settlement amounts for asbestos-related lawsuits and claims is as follows:

| (\$ in thousands)                                      | 13 Weeks Ended<br>February 26, 2011 | 13 Weeks Ended<br>February 27, 2010 |
|--|-------------------------------------|-------------------------------------|
| Lawsuits and claims settled                            | 2                                   | 2                                   |
| Settlements reached                                    | \$ 0.2                              | \$ 0.4                              |
| Insurance payments received or expected to be received | \$ 0.1                              | \$ 0.3                              |

We do not believe that it would be meaningful to disclose the aggregate number of asbestos-related lawsuits filed against us because relatively few of these lawsuits are known to involve exposure to asbestos-containing products that we manufactured. Rather, we believe it is more meaningful to disclose the number of lawsuits that are settled and result in a payment to the plaintiff.

To the extent we can reasonably estimate the amount of our probable liabilities for pending asbestos-related claims, we establish a financial provision and a corresponding receivable for insurance recoveries. As of February 26, 2011, our probable liabilities and insurance recoveries related to asbestos claims were \$0.7 million and \$0.5 million, respectively. We have concluded that it is not possible to reasonably estimate the cost of disposing of other asbestos-related claims (including claims that might be filed in the future) due to our inability to project future events. Future variables include the number of claims filed or dismissed, proof of exposure to our products, seriousness of the alleged injury, the number and solvency of other defendants in each case, the jurisdiction in which the case is brought, the cost of disposing of such claims, the uncertainty of asbestos litigation, insurance coverage and indemnification agreement issues, and the continuing solvency of certain insurance companies.

Based on currently available information, we do not believe that asbestos-related litigation, individually or in aggregate, will have a material adverse effect on our long-term financial condition. However, adverse developments and/or periodic settlements in such litigation could negatively impact the results of operations or cash flows in one or more future quarters.

In addition to product liability claims discussed above, we are involved in other claims or legal proceedings related to our products, which we believe are not out of the ordinary in a business of the type and size in which we are engaged.

### Item 1A. Risk Factors

This Form 10-Q contains forward-looking statements concerning our future programs, products, expenses, revenue, liquidity and cash needs as well as our plans and strategies. These forward-looking statements are based on current expectations and we assume no obligation to update this information. Numerous factors could cause actual results to differ significantly from the results described in these forward-looking statements, including the risk factors identified under Part I, Item 1A. Risk Factors contained in our Annual Report on Form 10-K for the fiscal year ended November 27, 2010. There have been no material changes in the risk factors disclosed by us under Part I, Item 1A. Risk Factors contained in the Annual Report on Form 10-K for the fiscal year ended November 27, 2010.

### Item 1B. Unresolved Staff Comments

None.

## Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

### Issuer Purchases of Equity Securities

Information on our purchases of equity securities during the first quarter follows:

| Period                               | (a)<br>Total<br>Number of<br>Shares<br>Purchased <sup>1</sup> | (b)<br>Average<br>Price Paid<br>per Share | (c)<br>Total Number<br>of<br>Shares<br>Purchased as<br>Part of a<br>Publicly<br>Announced Plan<br>or Program | (d)<br>Maximum<br>Approximate<br>Dollar<br>Value of Shares that<br>may yet be<br>Purchased Under the<br>Plan or Program<br>(thousands) |
|--------------------------------------|---|---|--|--|
| November 28, 2010 - January 1, 2011  | 29,142  | \$ 21.59                                  |  | \$ 100,000   |
| January 2, 2011 - January 29, 2011   | 109,600   | \$ 22.79                                  | 109,600  | \$ 97,503  |
| January 30, 2011 - February 26, 2011 |   | \$  |  | \$ 97,503  |

Repurchases of common stock are made to support our stock-based employee compensation plans and for other corporate purposes.

Upon vesting of restricted stock awarded to employees, shares are withheld to cover the employees' withholding taxes. On September 30, 2010, the Board of Directors authorized a new share repurchase program of up to \$100 million of our outstanding common shares. Under the program, we are authorized to repurchase shares for cash on the open market, from time to time, in privately negotiated transactions or block transactions, or through an accelerated repurchase agreement. The timing of such repurchases is dependent on price, market conditions and applicable regulatory requirements. Upon repurchase of the shares, we reduced our common stock for the par value of the shares with the excess being applied against additional paid-in capital.

<sup>1</sup> The total number of shares purchased includes: (i) shares purchased under the board's authorization described above and (ii) shares withheld to satisfy the employees' withholding taxes upon vesting of restricted stock. There were 29,142 shares withheld in the first quarter of 2011 to satisfy employee tax withholdings.



**Item 6. Exhibits**

- 31.1 Form of 302 Certification James J. Owens
- 31.2 Form of 302 Certification James R. Giertz
- 32.1 Form of 906 Certification James J. Owens
- 32.2 Form of 906 Certification James R. Giertz
- 101 The following materials from the H.B. Fuller Company Quarterly Report on Form 10-Q for the quarter ended February 26, 2011 formatted in Extensible Business Reporting Language (XBRL): (i) the Consolidated Statements of Income, (ii) the Consolidated Balance Sheets, (iii) the Consolidated Statement of Cash Flows and (v) the Notes to Consolidated Financial Statements, tagged as blocks of text.

**SIGNATURES**

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

**H.B. Fuller Company**

Dated: March 28, 2011

/s/ James R. Giertz  
James R. Giertz  
Senior Vice President,  
Chief Financial Officer

**Exhibit Index**

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