

ROCK TENN CO  
Form 10-Q  
May 14, 2004

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

**Form 10-Q**

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

For the quarterly period ended **March 31, 2004**

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 0-23340

**Rock-Tenn Company**

(Exact name of registrant as specified in its charter)

Georgia  
(State or other jurisdiction of  
incorporation or organization)

62-0342590  
(I.R.S. Employer  
Identification No.)

504 Thrasher Street, Norcross,  
Georgia  
(Address of principal executive  
offices)

30071  
(Zip Code)

Registrant's telephone number, including area code: (770) 448-2193

N/A

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

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes x No o

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

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| Class                                  | Outstanding as of May 5,<br>2004 |
|--|----------------------------------|
| Class A Common Stock, \$0.01 par value | 35,408,724                       |

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**Table of Contents****PART I: FINANCIAL INFORMATION****Item 1. Financial Statements (Unaudited)****ROCK-TENN COMPANY****CONDENSED CONSOLIDATED STATEMENTS OF INCOME**  
**(Unaudited) (In Thousands, Except Per Share Data)**

|  | <b>Three Months Ended</b> |                  | <b>Six Months Ended</b> |                  |
|--|---------------------------|------------------|-------------------------|------------------|
|  | <b>March 31,</b>          | <b>March 31,</b> | <b>March 31,</b>        | <b>March 31,</b> |
|  | <b>2004</b>               | <b>2003</b>      | <b>2004</b>             | <b>2003</b>      |
| Net sales  | \$400,000                 | \$350,234        | \$766,110               | \$680,083        |
| Cost of goods sold   | 331,594                   | 287,071          | 635,938                 | 554,992          |
| Gross profit   | 68,406                    | 63,163           | 130,172                 | 125,091          |
| Selling, general and administrative expenses   | 51,094                    | 42,991           | 99,083                  | 90,012           |
| Restructuring and other costs  | 6,043                     | 935              | 6,175                   | 416              |
| Operating profit   | 11,269                    | 19,237           | 24,914                  | 34,663           |
| Interest expense   | (5,871)                   | (6,566)          | (11,782)                | (13,029)         |
| Interest and other income  | 132                       | 56               | 212                     | 108              |
| Loss from unconsolidated joint venture   | (83)                      | (284)            | (133)                   | (284)            |
| Minority interest in income of consolidated subsidiary   | (590)                     | (784)            | (1,476)                 | (1,522)          |
| Income from continuing operations before income taxes  | 4,857                     | 11,659           | 11,735                  | 19,936           |
| Provision for income taxes   | 1,848                     | 4,528            | 4,560                   | 7,860            |
| Income from continuing operations  | 3,009                     | 7,131            | 7,175                   | 12,076           |
| Income (loss) from discontinued operations (net of \$(48), \$125, \$4,665, and \$204 income taxes) | (99)                      | 199              | 7,614                   | 324              |
| Net income   | \$ 2,910                  | \$ 7,330         | \$ 14,789               | \$ 12,400        |
| Weighted average number of common and common equivalent shares outstanding                         | 35,312                    | 34,515           | 35,305                  | 34,513           |

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|                                   |                   |                   |                   |                   |
|-----------------------------------|-------------------|-------------------|-------------------|-------------------|
| Basic earnings per share:         |                   |                   |                   |                   |
| Income from continuing operations | \$ 0.09           | \$ 0.21           | \$ 0.21           | \$ 0.35           |
|                                   | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u> |
| Net income                        | \$ 0.08           | \$ 0.21           | \$ 0.43           | \$ 0.36           |
|                                   | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u> |
| Diluted earnings per share:       |                   |                   |                   |                   |
| Income from continuing operations | \$ 0.09           | \$ 0.21           | \$ 0.20           | \$ 0.35           |
|                                   | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u> |
| Net income                        | \$ 0.08           | \$ 0.21           | \$ 0.42           | \$ 0.36           |
|                                   | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u> |
| Cash dividends per common share   | \$ 0.085          | \$ 0.08           | \$ 0.17           | \$ 0.16           |
|                                   | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u> |

See Accompanying Notes to Condensed Consolidated Financial Statements

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Table of Contents**ROCK-TENN COMPANY****CONDENSED CONSOLIDATED BALANCE SHEETS**  
**(Unaudited) (In Thousands, Except Share And Per Share Data)**

|  | <b>March 31,<br/>2004</b> | <b>September 30,<br/>2003</b> |
|--|---------------------------|-------------------------------|
|  | <hr/>                     | <hr/>                         |
| <b>ASSETS</b>  |                           |                               |
| Current assets:  |                           |                               |
| Cash and cash equivalents                                      | \$ 73,216                 | \$ 14,173                     |
| Accounts receivable (net of allowances of \$5,821 and \$5,475) | 168,539                   | 163,096                       |
| Inventories  | 120,568                   | 118,414                       |
| Other current assets   | 13,163                    | 17,717                        |
| Current assets held for sale                                   |                           | 52,703                        |
|  | <hr/>                     | <hr/>                         |
| Total current assets   | 375,486                   | 366,103                       |
| Property, plant and equipment at cost:                         |                           |                               |
| Land and buildings   | 220,386                   | 226,153                       |
| Machinery and equipment  | 967,955                   | 946,050                       |
| Transportation equipment                                       | 8,375                     | 8,408                         |
| Leasehold improvements   | 5,769                     | 5,713                         |
|  | <hr/>                     | <hr/>                         |
|  | 1,202,485                 | 1,186,324                     |
| Less accumulated depreciation and amortization                 | (634,685)                 | (606,810)                     |
|  | <hr/>                     | <hr/>                         |
| Net property, plant and equipment                              | 567,800                   | 579,514                       |
| Goodwill   | 295,805                   | 291,799                       |
| Intangibles, net   | 18,357                    | 21,843                        |
| Other assets   | 32,211                    | 32,136                        |
|  | <hr/>                     | <hr/>                         |
|  | \$1,289,659               | \$1,291,395                   |
|  | <hr/>                     | <hr/>                         |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>                     |                           |                               |
| Current liabilities:   |                           |                               |
| Accounts payable   | \$ 80,478                 | \$ 84,151                     |
| Accrued compensation and benefits                              | 42,522                    | 46,935                        |
| Current maturities of debt                                     | 414                       | 12,927                        |
| Other current liabilities                                      | 38,191                    | 35,983                        |
| Current liabilities held for sale                              |                           | 7,487                         |
|  | <hr/>                     | <hr/>                         |
| Total current liabilities                                      | 161,605                   | 187,483                       |

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|  |                   |                   |
|--|-------------------|-------------------|
| Long-term debt due after one year  | 488,907           | 489,037           |
| Realized interest rate swap gains  | 23,979            | 24,024            |
| Mark-to-market value of interest rate swaps  | 1,094             | (94)              |
|  | <u>          </u> | <u>          </u> |
| Total long-term debt, less current maturities  | 513,980           | 512,967           |
| Deferred income taxes  | 89,413            | 93,801            |
| Other long-term items  | 86,050            | 75,108            |
| Shareholders' equity:  |                   |                   |
| Preferred stock, \$0.01 par value; 50,000,000 shares authorized; no shares outstanding   |                   |                   |
| Class A common stock, \$0.01 par value; 175,000,000 shares authorized; 35,183,239 and 34,962,041 shares outstanding at March 31, 2004 and September 30, 2003, respectively | 352               | 350               |
| Capital in excess of par value   | 152,694           | 149,722           |
| Deferred compensation  | (2,543)           | (3,105)           |
| Retained earnings  | 324,725           | 315,905           |
| Accumulated other comprehensive loss   | (36,617)          | (40,836)          |
|  | <u>          </u> | <u>          </u> |
| Total shareholders' equity   | 438,611           | 422,036           |
|  | <u>          </u> | <u>          </u> |
|  | \$1,289,659       | \$1,291,395       |
|  | <u>          </u> | <u>          </u> |

See Accompanying Notes to Condensed Consolidated Financial Statements



Table of Contents**ROCK-TENN COMPANY****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(Unaudited) (In Thousands)**

|   | <b>Six Months Ended</b>   |                           |
|---|---------------------------|---------------------------|
|   | <b>March 31,<br/>2004</b> | <b>March 31,<br/>2003</b> |
|   | <hr/>                     | <hr/>                     |
| <b>Operating activities:</b>  |                           |                           |
| Income from continuing operations   | \$ 7,175                  | \$ 12,076                 |
| Items in income not affecting cash:   |                           |                           |
| Depreciation and amortization   | 37,159                    | 35,455                    |
| Deferred income taxes   | (4,388)                   | 652                       |
| Income tax benefit of employee stock options                                  | 188                       |                           |
| Deferred compensation expense   | 562                       | 342                       |
| Gain on disposal of plant and equipment and other, net                        | (2,170)                   | (741)                     |
| (Gain) loss on currency translation   | (241)                     | 15                        |
| Minority interest in income of consolidated subsidiary                        | 1,476                     | 1,522                     |
| Equity in loss from joint venture   | 133                       | 284                       |
| Pension funding less than expense   | 8,697                     | 5,867                     |
| Impairment loss and other non-cash charges                                    | 6,945                     | 881                       |
| Change in operating assets and liabilities:                                   |                           |                           |
| Accounts receivable   | (5,528)                   | 10,643                    |
| Inventories   | (2,710)                   | 843                       |
| Other assets  | (2,337)                   | (279)                     |
| Accounts payable  | (5,404)                   | (614)                     |
| Accrued liabilities   | (4,883)                   | (18,252)                  |
|   | <hr/>                     | <hr/>                     |
| Cash provided by operating activities from continuing operations              | 34,674                    | 48,694                    |
| Cash provided by operating activities from discontinued operations            | 451                       | 2,914                     |
|   | <hr/>                     | <hr/>                     |
| Net cash provided by operating activities                                     | 35,125                    | 51,608                    |
| <b>Investing activities:</b>  |                           |                           |
| Capital expenditures  | (30,344)                  | (31,395)                  |
| Cash paid for purchase of businesses, net of cash received                    | (1,094)                   | (65,220)                  |
| Cash contributed to joint venture   | (103)                     | (237)                     |
| Proceeds from sale of property, plant and equipment                           | 5,178                     | 6,693                     |
|   | <hr/>                     | <hr/>                     |
| Cash used for investing activities from continuing operations                 | (26,363)                  | (90,159)                  |
| Cash provided by (used for) investing activities from discontinued operations | 61,921                    | (591)                     |
|   | <hr/>                     | <hr/>                     |
| Net cash provided by (used for) investing activities                          | 35,558                    | (90,750)                  |

**Financing activities:**

|   |                   |                   |
|---|-------------------|-------------------|
| Proceeds from issuance of public notes                    |                   | 99,748            |
| Net additions (repayments) to revolving credit facilities | (3,500)           | 1,600             |
| Additions to long-term debt                               | 54                | 23,878            |
| Repayments of long-term debt                              | (9,246)           | (82,976)          |
| Proceeds from monetizing swap contracts                   | 4,169             | 2,482             |
| Decrease in unexpended industrial revenue bond proceeds   |                   | 827               |
| Issuances of common stock                                 | 2,785             | 1,981             |
| Debt issuance costs                                       |                   | (990)             |
| Purchases of common stock                                 |                   | (1,313)           |
| Cash dividends paid to shareholders                       | (5,969)           | (5,508)           |
| Distribution to minority interest                         | (350)             | (1,260)           |
|   | <u>          </u> | <u>          </u> |
| Cash provided by (used for) financing activities          | (12,057)          | 38,469            |
| Effect of exchange rate changes on cash                   | 417               | (368)             |
|   | <u>          </u> | <u>          </u> |
| Increase (decrease) in cash and cash equivalents          | 59,043            | (1,041)           |
| Cash and cash equivalents at beginning of period          | 14,173            | 6,560             |
|   | <u>          </u> | <u>          </u> |
| Cash and cash equivalents at end of period                | \$ 73,216         | \$ 5,519          |
|   | <u>          </u> | <u>          </u> |
| Supplemental disclosure of cash flow information:         |                   |                   |
| Cash paid during the period for:                          |                   |                   |
| Income taxes, net of refunds                              | \$ 10,554         | \$ 7,190          |
| Interest, net of amounts capitalized                      | 17,275            | 12,293            |

See Accompanying Notes to Condensed Consolidated Financial Statements

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**ROCK-TENN COMPANY**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)**  
**(Unaudited)**  
**(In Thousands)**

Supplemental schedule of non-cash investing and financing activities:

In the first six months of fiscal 2004, we paid \$1,094, primarily for additional consideration due to the August 2003 acquisition of PCPC, Inc., d/b/a Pacific Coast Packaging Corp. (which we refer to as **Pacific Coast Packaging** ). The payment represented an adjustment based on the achievement of certain sales levels for the six-month period following the closing of the transaction and was recorded as goodwill. In the first six months of fiscal 2003, the Company paid \$65,220 for the purchase of Groupe Cartem Wilco Inc. (which we refer to as **Cartem Wilco** ). In conjunction with the acquisitions, liabilities were assumed as follows:

|  | <b>Six Months Ended</b>       |                           |
|--|-------------------------------|---------------------------|
|  | <b>March<br/>31,<br/>2004</b> | <b>March 31,<br/>2003</b> |
| Fair value of assets acquired including goodwill | \$ 1,094                      | \$ 77,654                 |
| Cash paid  | 1,094                         | 65,220                    |
|  | <u>          </u>             | <u>          </u>         |
| Liabilities assumed                              | \$                            | \$ 12,434                 |
|  | <u>          </u>             | <u>          </u>         |

See Accompanying Notes to Condensed Consolidated Financial Statements

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**ROCK-TENN COMPANY**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**For the Three Month Period Ended March 31, 2004 (Unaudited)**

*Unless the context otherwise requires, we, us, our or the Company refers to the business of Rock-Tenn Company and its subsidiaries, including RTS Packaging, LLC, which we refer to as **RTS**, and Seven Hills Paperboard, LLC, which we refer to as **Seven Hills**. We own 65% of RTS and conduct our interior packaging products business through RTS. We own 49% of Seven Hills, a manufacturer of gypsum plasterboard liner, which we do not consolidate for purposes of our financial statements.*

**Note 1. Interim Financial Statements**

The accompanying condensed consolidated financial statements of the Company have not been audited by independent auditors. The condensed consolidated balance sheet at September 30, 2003 has been derived from the audited consolidated financial statements. In the opinion of our management, the condensed consolidated financial statements reflect all adjustments, which are of a normal recurring nature, necessary for a fair presentation of the results of operations for the three and six month periods ended March 31, 2004 and 2003, the Company's financial position at March 31, 2004 and September 30, 2003, and the cash flows for the six month periods ended March 31, 2004 and 2003.

Certain notes and other information have been condensed or omitted from the interim financial statements presented in this Quarterly Report on Form 10-Q. Therefore, these financial statements should be read in conjunction with the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2003 (the **Fiscal 2003 Form 10-K**).

The results for the three and six months ended March 31, 2004 are not necessarily indicative of results that may be expected for the full year.

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

**Note 2. New Accounting Standards**

In December 2003, the Financial Accounting Standards Board (which we refer to as the **FASB**) released revised FASB Statement

No. 132(R), *Employers' Disclosures about Pensions and Other Postretirement Benefits* (which we refer to as **SFAS 132R**). We adopted this standard as of January 1, 2004. SFAS 132R requires additional disclosures to those required in the original SFAS 132 about the assets, obligations, cash flows and net periodic benefit costs of defined benefit pension plans and other defined benefit postretirement plans, including new disclosures in interim financial reports. We have included the new interim disclosures in Note 12 to the Condensed Consolidated Financial Statements. The adoption of SFAS 132R did not have a material effect on our consolidated financial statements.

In December 2003, the FASB issued revised FASB Interpretation No. 46(R), *Consolidation of Variable Interest Entities, an Interpretation of ARB 51* (which we refer to as **FIN 46R**). We adopted this interpretation on March 31, 2004 for any variable interest entities (which we refer to as **VIEs**) in which we hold a variable interest that we acquired before February 1, 2003. We have not acquired any variable interests since that date. The only VIE in which we believe we hold a variable interest in is discussed in Note 3 to the Condensed Consolidated Financial Statements under the heading **Investment in Corporate Joint Venture**.



**Table of Contents****Note 3. Summary of Significant Accounting Policies**

The following significant accounting policies have been revised since we filed our Fiscal 2003 Form 10-K to more clearly reflect our accounting for these items. Except for our adoption of FIN 46R, none of these changes represent a change in accounting principle or policy.

***Investment in Corporate Joint Venture***

During 2000, the Company formed a joint venture ( **Seven Hills** or the **Joint Venture** ) with Lafarge North America, Inc. ( **Lafarge** ). The Company contributed cash and a paper machine located at its Lynchburg, Virginia paper mill. Lafarge contributed cash. Subsequent to inception the Company and Lafarge have made additional cash contributions. The Company has invested a total of \$22.9 million in Seven Hills as of March 31, 2004. The Company uses the equity method to account for its 49% investment in Seven Hills. Under the equity method, the Company's investment was initially recorded at cost, then subsequently reduced by distributions and increased or decreased by the Company's proportionate share of the Joint Venture's net earnings or loss. Funding of net losses is guaranteed by the partners of the joint venture in relation to their proportionate share of ownership. Under the terms of the Seven Hills joint venture arrangement, Lafarge is required to purchase all of the gypsum plasterboard liner produced by Seven Hills. Seven Hills is managed by a Managing Board that has equal representation by Lafarge and the Company. The Company provides all labor, supervision, management, executive and administrative services necessary to operate Seven Hills and leases the land and building occupied by Seven Hills. Our share of cumulative losses as of March 31, 2004 and 2003 are \$1.8 million and \$1.6 million, respectively. Under the terms of the joint venture agreement, Lafarge has the option to put, at an amount determined by a formula, its interest in the Joint Venture to the Company at any time after the expiration of six years from March 29, 2001, the date that the Joint Venture's paper machine was converted to produce gypsum plasterboard liner. Upon the adoption of FIN 46R on March 31, 2004 (see Note 2 above), the Company determined the Joint Venture is a VIE, but the Company is not its primary beneficiary. Accordingly, we will continue to account for Seven Hills using the equity method.

***Revenue Recognition***

We recognize revenue when all of the following criteria, which are detailed in Codification of Staff Accounting Bulletins, Topic 13:A.1, *Revenue Recognition-General*, are met:

Persuasive evidence that an arrangement exists.

Delivery has occurred or services have been rendered.

The seller's price to the buyer is fixed or determinable.

Collectibility is reasonably assured.

Items that we net against our gross revenue include provisions for discounts, returns, allowances, customer rebates, outbound freight billed to customers and other adjustments. We account for such provisions during the same period in which we record the related revenues, except for changes in the fair value of derivatives, which we recognize as described below, and expense for cash discounts are recorded as earned when payments are received from our customers.

***Derivatives***

The Company enters into a variety of derivative transactions. The Company uses swap agreements to manage the interest rate characteristics of a portion of its outstanding debt. The Company uses forward contracts to limit exposure

to fluctuations in Canadian foreign currency rates with respect to its receivables denominated in Canadian dollars. The Company also uses commodity swap agreements to limit exposure to falling sales prices and rising raw material costs. The Company is exposed to counterparty credit risk for nonperformance and, in the event of nonperformance, to market risk for changes in interest rates. The Company manages exposure to counterparty credit risk through minimum credit standards, diversification of counterparties and procedures to monitor concentrations of credit risk.

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For each derivative instrument that is designated and qualifies as a fair value hedge, the gain or loss on the derivative instrument as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in current earnings during the period of the changes in fair values. For each derivative instrument that is designated and qualifies as a cash flow hedge, the effective portion of the gain or loss on the derivative instrument is reported as a component of accumulated other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. The ineffective portion of the hedge is recognized in current earnings during the period of change. Gains or losses on the termination of interest rate swap agreements are deferred and amortized as an adjustment to interest expense of the related debt instrument over the remaining term of the original contract life of the terminated swap agreements. For derivative instruments not designated as hedging instruments, the gain or loss is recognized in current earnings during the period of change. The fair value of the Company's derivative instruments are based on market quotes and represents the net amount required to terminate the position, taking into consideration market rates and counterparty credit risk. Derivative contracts that are an asset from the Company's perspective are reported as other assets. Contracts that are liabilities from the Company's perspective are recorded as other liabilities.

**Note 4. Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates and the differences could be material.

The most significant accounting estimates inherent in the preparation of the Company's financial statements include estimates associated with its evaluation of the recoverability of goodwill and property, plant and equipment as well as those used in the determination of taxation, insurance and restructuring. In addition, significant estimates form the basis for the Company's reserves with respect to collectibility of accounts receivable, inventory valuations, pension benefits, and certain benefits provided to current employees. Various assumptions and other factors underlie the determination of these significant estimates. The process of determining significant estimates is fact specific and takes into account factors such as historical experience, current and expected economic conditions, product mix, and in some cases, actuarial techniques. We constantly re-evaluate these significant factors and make adjustments where facts and circumstances dictate.

**Note 5. Comprehensive Income**

The following are the components of comprehensive income (in thousands):

|  | <b>Three Months Ended</b> |                  | <b>Six Months Ended</b> |                  |
|--|---------------------------|------------------|-------------------------|------------------|
|  | <b>March 31,</b>          | <b>March 31,</b> | <b>March 31,</b>        | <b>March 31,</b> |
|  | <b>2004</b>               | <b>2003</b>      | <b>2004</b>             | <b>2003</b>      |
| Net income                                       | \$ 2,910                  | \$ 7,330         | \$14,789                | \$12,400         |
| Foreign currency translation adjustment          | (1,865)                   | 6,148            | 4,191                   | 6,730            |
| Unrealized gain (loss) on derivative instruments | (267)                     | (227)            | 28                      | (102)            |
| Total other comprehensive income (loss)          | (2,132)                   | 5,921            | 4,219                   | 6,628            |



|                      |                   |                   |                   |                   |
|----------------------|-------------------|-------------------|-------------------|-------------------|
| Comprehensive income | \$ 778            | \$13,251          | \$19,008          | \$19,028          |
|                      | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u> |

The change in other comprehensive income is primarily due to the fluctuation in the Canadian/U.S. exchange rate and an increase in our overall investment in Canada as a result of our acquisition of Cartem Wilco in January 2003. The second quarter of fiscal 2004 was impacted as the exchange rate moved to 1.3111 at March 31, 2004 from 1.2963 at December 31, 2003. The second quarter of fiscal 2003 was impacted as the exchange rate moved to 1.4699 at March 31, 2003 from 1.5723 at December 31, 2003.

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The six months ended March 31, 2004 was impacted as the exchange rate moved to 1.3111 at March 31, 2004 from 1.3493 at September 30, 2003. The six months ended March 31, 2003 was impacted as the exchange rate moved to 1.4699 at March 31, 2003 from 1.5870 at September 30, 2002.

**Note 6. Earnings per Share**

The following table sets forth the computation of basic and diluted earnings per share (in thousands, except per share data):

|  | <b>Three Months Ended</b> |                           | <b>Six Months Ended</b>   |                           |
|--|---------------------------|---------------------------|---------------------------|---------------------------|
|  | <b>March 31,<br/>2004</b> | <b>March 31,<br/>2003</b> | <b>March 31,<br/>2004</b> | <b>March 31,<br/>2003</b> |
| Numerator:   |                           |                           |                           |                           |
| Income from continuing operations  | \$ 3,009                  | \$ 7,131                  | \$ 7,175                  | \$12,076                  |
| Income (loss) from discontinued operations,<br>net of tax  | (99)                      | 199                       | 7,614                     | 324                       |
|  | <u>          </u>         | <u>          </u>         | <u>          </u>         | <u>          </u>         |
| Net income   | \$ 2,910                  | \$ 7,330                  | \$14,789                  | \$12,400                  |
|  | <u>          </u>         | <u>          </u>         | <u>          </u>         | <u>          </u>         |
| Denominator:   |                           |                           |                           |                           |
| Denominator for basic earnings per share<br>weighted average shares                              | 34,830                    | 34,203                    | 34,771                    | 34,184                    |
| Effect of dilutive stock options and<br>restricted stock awards                                  | 482                       | 312                       | 534                       | 329                       |
|  | <u>          </u>         | <u>          </u>         | <u>          </u>         | <u>          </u>         |
| Denominator for diluted earnings per share<br>weighted average shares and assumed<br>conversions | 35,312                    | 34,515                    | 35,305                    | 34,513                    |
|  | <u>          </u>         | <u>          </u>         | <u>          </u>         | <u>          </u>         |
| Basic earnings per share:  |                           |                           |                           |                           |
| Income from continuing operations  | \$ 0.09                   | \$ 0.21                   | \$ 0.21                   | \$ 0.35                   |
| Income (loss) from discontinued operations,<br>net of tax  | (0.01)                    |                           | 0.22                      | 0.01                      |
|  | <u>          </u>         | <u>          </u>         | <u>          </u>         | <u>          </u>         |
| Net income per share basic   | \$ 0.08                   | \$ 0.21                   | \$ 0.43                   | \$ 0.36                   |
|  | <u>          </u>         | <u>          </u>         | <u>          </u>         | <u>          </u>         |
| Diluted earnings per share:  |                           |                           |                           |                           |
| Income from continuing operations  | \$ 0.09                   | \$ 0.21                   | \$ 0.20                   | \$ 0.35                   |
|  | (0.01)                    |                           | 0.22                      | 0.01                      |

Income (loss) from discontinued operations,  
net of tax

|                                 |         |         |         |         |
|---------------------------------|---------|---------|---------|---------|
|                                 | _____   | _____   | _____   | _____   |
| Net income per share    diluted | \$ 0.08 | \$ 0.21 | \$ 0.42 | \$ 0.36 |
|                                 | _____   | _____   | _____   | _____   |

#### Note 7. Restructuring and Other Costs

We recorded pre-tax restructuring and other costs of \$6.0 million and \$6.2 million for the second quarter of fiscal 2004 and the six months ending March 31, 2004, respectively. We recorded pre-tax charges of \$0.9 million and \$0.4 million for the second quarter of fiscal 2003 and the six months ending March 31, 2003, respectively. These charges are discussed below.

During the second quarter of fiscal 2004, we announced the closure of our Wright City, Missouri laminated paperboard facility effective March 31, 2004 and recorded a pre-tax charge of \$7.7 million. The charge consisted of an asset impairment charge of \$6.5 million to record the equipment and facility at their estimated fair value less cost to sell, a goodwill impairment charge of \$0.2 million, severance and other employee costs of \$0.4 million, inventory write-off of \$0.4 million, and other costs of \$0.2 million. The closure resulted in the termination of approximately 68 employees. Net sales at the facility for the six-month period ended March 31, 2004 and March 31, 2003 were \$5.1 million and \$6.7 million, respectively. Operating losses at the facility for the same six-month periods were \$1.6 million and \$1.9 million, respectively. We do not anticipate consolidating the majority of the sales of this operation into our remaining laminated facilities. We also sold our previously closed Mundelein, Illinois merchandising display facility site for a pre-tax gain of \$1.8 million. In addition, we recorded a variety of charges from previously announced closures totaling \$0.1 million in the period.

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During the six months ended March 31, 2004, we recorded a pre-tax charge of \$7.7 million for the closure of our Wright City facility, recorded a \$1.8 million pre-tax gain on the sale of our Mundelein facility, and incurred a variety of charges from previously announced closures totaling \$0.3 million. The charges from the previously announced closings consisted primarily of \$0.1 million for equipment relocation, \$0.1 million for inventory write-off, and \$0.1 million of carrying costs.

The following table represents a summary of the restructuring accrual as well as a reconciliation of the restructuring accrual to the line item "**Restructuring and other costs**" on the condensed consolidated statements of income for the six months ended March 31, 2004 (in thousands):

|  | <b>Reserve at<br/>September<br/>30, 2003</b> | <b>Restructuring<br/>Charges</b> | <b>Payments</b>   | <b>Adjustment<br/>to<br/>Accrual</b> | <b>Reserve at<br/>March 31,<br/>2004</b> |
|--|--|----------------------------------|-------------------|--------------------------------------|--|
| Severance and other employee costs               | \$ 160                                       | \$ 425                           | \$(140)           | \$                                   | \$ 445                                   |
| Other  | 10   | 100                              | (9)               | —                                    | 101                                      |
|  | <u>          </u>                            | <u>          </u>                | <u>          </u> | <u>          </u>                    | <u>          </u>                        |
| Total Restructuring                              | \$ 170                                       | \$ 525                           | \$(149)           | \$                                   | \$ 546                                   |
|  | <u>          </u>                            |                                  | <u>          </u> | <u>          </u>                    | <u>          </u>                        |
| Property, plant and equipment<br>impairment loss |  | 6,466                            |                   |                                      |  |
| Gain on sale of property, plant and<br>equipment |  | (1,830)                          |                   |                                      |  |
| Equipment relocation                             |  | 94                               |                   |                                      |  |
| Inventory write-off                              |  | 479                              |                   |                                      |  |
| Goodwill impairment                              |  | 244                              |                   |                                      |  |
| Carrying costs                                   |  | 64                               |                   |                                      |  |
| Other  |  | 133                              |                   |                                      |  |
|  |  | <u>          </u>                |                   |                                      |  |
| Total restructuring and other costs              |  | \$ 6,175                         |                   |                                      |  |
|  |  | <u>          </u>                |                   |                                      |  |

During the second quarter of fiscal 2003, we recorded a pre-tax charge of \$0.9 million. In that quarter, we announced the closure of our Hunt Valley, Maryland and Mundelein merchandising displays facilities. The closures resulted in the termination of approximately 49 employees. In connection with these closings, we accrued \$0.1 million for severance and other employee costs. These facilities were consolidated into the operations of other existing facilities. The other \$0.8 million consisted primarily of the following: \$0.7 million for equipment relocation charges primarily consisting of \$0.3 million at our El Paso, Texas folding carton facility and \$0.3 million at our Vineland, New Jersey converting operation; \$0.2 million of inventory write-offs at our Dothan, Alabama corrugated facility; \$0.1 million for an accrual adjustment related to severance at our El Paso facility; a net gain of \$0.3 million for equipment sales primarily of folding carton equipment at our St. Paul, Minnesota folding carton facility; and miscellaneous other items at a variety of locations totaling \$0.1 million.

During the six months ended March 31, 2003, we recorded a pre-tax charge of \$0.4 million. The charge of \$0.4 million was net of a gain for accrual adjustments of \$1.0 million on previously announced facility closings. The \$1.0 million gain resulted from \$0.6 million in excess employee severance and other employee benefits due to employee voluntary terminations and employees who worked longer than planned in the notice period; and \$0.4 million in accrual reversals resulting from the earlier than planned sales of property associated with our facilities in Augusta, Georgia (\$0.1 million), Dothan, Alabama (\$0.1 million) and Vineland, New Jersey (\$0.2 million). Partially offsetting these accrual adjustments were \$1.2 million of equipment relocation expenses consisting primarily of \$0.7 million for Vineland, \$0.3 million for El Paso, and \$0.1 million for Dothan; \$0.2 million for an accrual adjustment for severance at our El Paso facility; \$0.1 million in severance adjustments for our Hunt Valley and Mundelein facilities; \$0.2 million of inventory write-offs at Dothan; a \$0.2 million net charge for the removal and ultimate sale of certain equipment in our St. Paul facility, a net gain on the sale of our Vineland property and equipment of \$0.5 million, and a charge of \$0.2 million for the loss on the sale of our Augusta property and equipment.

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The following table represents a summary of the restructuring accrual as well as a reconciliation of the restructuring accrual to the line item "**Restructuring and other costs**" on the condensed consolidated statements of income for the six months ended March 31, 2003 (in thousands):

|   | <b>Reserve at<br/>September<br/>30, 2002</b> | <b>Restructuring</b> |                   | <b>Adjustment<br/>to Accrual</b> | <b>Reserve at<br/>March 31,<br/>2003</b> |
|---|--|----------------------|-------------------|----------------------------------|--|
|   | <u>          </u>                            | <b>Charges</b>       | <b>Payments</b>   | <u>          </u>                | <u>          </u>                        |
| Severance and other<br>employee costs                             | \$ 2,560                                     | \$ 96                | \$(2,216)         | \$ (324)                         | \$ 116                                   |
| Facility carrying costs   | 770  |                      | (194)             | (434)                            | 142                                      |
| Other   | 605  |                      | (274)             | (270)                            | 61                                       |
|   | <u>          </u>                            | <u>          </u>    | <u>          </u> | <u>          </u>                | <u>          </u>                        |
| Total Restructuring   | \$ 3,935                                     | \$ 96                | \$(2,684)         | \$(1,028)                        | \$ 319                                   |
|   | <u>          </u>                            |                      | <u>          </u> | <u>          </u>                | <u>          </u>                        |
| Adjustment to accrual   |  | (1,028)              |                   |                                  |  |
| Property, plant and equipment<br>impairment loss and gain on sale |  | (273)                |                   |                                  |  |
| Equipment relocation  |  | 1,160                |                   |                                  |  |
| Inventory write-off   |  | 153                  |                   |                                  |  |
| Other   |  | 308                  |                   |                                  |  |
|   |  | <u>          </u>    |                   |                                  |  |
| Total restructuring and<br>other costs                            |  | \$ 416               |                   |                                  |  |
|   |  | <u>          </u>    |                   |                                  |  |

**Note 8. Discontinued Operations**

In the first quarter of fiscal 2004, we completed the sale of our plastic packaging division, and the sale of some of the assets and liabilities that we acquired in the January 2003 Cartem Wilco acquisition that were associated with a small folding carton and label plant in Quebec. The plastic packaging division transaction closed effective October 27, 2003 and we received proceeds of approximately \$59.0 million. As a result of the transaction, we recorded an after-tax gain of approximately \$7.1 million. The sale of some of the Cartem Wilco assets and liabilities, effective December 1, 2003, resulted in no gain or loss and we received proceeds of approximately \$2.9 million.

We expect to incur additional expenses totaling approximately \$0.2 million in the third and fourth quarter of fiscal 2004 primarily related to severance and other related employee costs for employees required to render future service as part of the plastic packaging division sale. We are expensing these costs ratably over the future service period, which is anticipated to expire in the fourth quarter of fiscal 2004. The plastic packaging sale transaction is subject to a final working capital adjustment, which we expect to complete in the third quarter of fiscal 2004. The adjustment is not expected to be material.

**Note 9. Stock Option Plans**

We have elected to follow Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* (which we refer to as **APB 25** ), and related interpretations in accounting for our employee stock options. Under APB 25, because the exercise price of our employee stock options equals the market price of the underlying stock on the date of grant, generally no compensation expense is recognized.

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Pro forma information regarding net income and earnings per share is required by Statement of Financial Accounting Standards No. 123, *Accounting for Stock-Based Compensation*, which also requires that the information be determined as if we had accounted for our employee stock options granted subsequent to September 30, 1995 under the fair value method of that statement. The fair values for the options granted subsequent to September 30, 1995 were estimated at the date of grant using a Black-Scholes option pricing model with the following weighted average assumptions:

|                         | <b>Three Months Ended<br/>March<br/>31,<br/>2004</b> | <b>March<br/>31,<br/>2003</b> | <b>Six Months Ended<br/>March<br/>31,<br/>2004</b> | <b>March<br/>31,<br/>2003</b> |
|-------------------------|--|-------------------------------|--|-------------------------------|
| Expected Term in Years  | 7  | 7                             | 7  | 7                             |
| Expected Volatility     | 44.0%  | 45.6%                         | 44.0%  | 45.7%                         |
| Risk-Free Interest Rate | 1.0%   | 1.1%                          | 1.0%   | 1.1%                          |
| Dividend Yield          | 2.2%   | 2.3%                          | 2.2%   | 2.4%                          |

  

|   | <b>Three Months Ended<br/>March<br/>31,<br/>2004</b> | <b>March<br/>31,<br/>2003</b> | <b>Six Months Ended<br/>March 31,<br/>2004</b> | <b>March 31,<br/>2003</b> |
|---|--|-------------------------------|--|---------------------------|
| Net income, as reported   | \$2,910  | \$7,330                       | \$14,789                                       | \$12,400                  |
| Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects | (812)  | (600)                         | (1,333)  | (1,207)                   |
| Pro forma net income  | <u>\$2,098</u>                                       | <u>\$6,730</u>                | <u>\$13,456</u>                                | <u>\$11,193</u>           |
| Earnings per share:   |  |                               |  |                           |
| Basic as reported   | <u>\$ 0.08</u>                                       | <u>\$ 0.21</u>                | <u>\$ 0.43</u>                                 | <u>\$ 0.36</u>            |
| Basic pro forma   | <u>\$ 0.06</u>                                       | <u>\$ 0.20</u>                | <u>\$ 0.39</u>                                 | <u>\$ 0.33</u>            |
| Diluted as reported   | <u>\$ 0.08</u>                                       | <u>\$ 0.21</u>                | <u>\$ 0.42</u>                                 | <u>\$ 0.36</u>            |
| Diluted pro forma   | <u>\$ 0.06</u>                                       | <u>\$ 0.20</u>                | <u>\$ 0.38</u>                                 | <u>\$ 0.32</u>            |

**Note 10. Inventories**



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Substantially all of our U.S. inventories are stated at the lower of cost or market, with cost determined on the last-in, first-out (LIFO) basis. All other inventories are valued at the lower of cost or market, with cost determined using methods that approximate cost computed on a first-in, first-out (FIFO) basis. An actual valuation of inventory under the LIFO method can only be made at the end of each year based on the inventory levels and costs at that time. Accordingly, interim LIFO estimates must necessarily be based on management's projection of expected year-end inventory levels and costs.

Inventories at March 31, 2004 and September 30, 2003 were as follows (in thousands):

|                                    | <b>March 31,<br/>2004</b>   | <b>September 30,<br/>2003</b> |
|------------------------------------|-----------------------------|-------------------------------|
|                                    | <u>                    </u> | <u>                    </u>   |
| Finished goods and work in process | \$ 94,880                   | \$ 91,751                     |
| Raw materials                      | 37,309                      | 37,675                        |
| Supplies                           | <u>13,394</u>               | <u>13,246</u>                 |
| <br>                               |                             |                               |
| Inventories at FIFO cost           | 145,583                     | 142,672                       |
| LIFO reserve                       | <u>(25,015)</u>             | <u>(24,258)</u>               |
| <br>                               |                             |                               |
| Net inventories                    | <u>\$ 120,568</u>           | <u>\$ 118,414</u>             |

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Debt, excluding the realized interest rate swap gains and the mark-to-market value of interest rate swaps totaling \$25.1 million and \$23.9 million at March 31, 2004 and September 30, 2003, respectively, consists of the following (in thousands):

|   | <b>March 31,<br/>2004</b> | <b>September<br/>30,<br/>2003</b> |
|---|---------------------------|-----------------------------------|
|   | <hr/>                     | <hr/>                             |
| 5.625% notes, due March 2013, net of unamortized discount of \$226 and \$238 <sup>(a)</sup>   | \$ 99,774                 | \$ 99,762                         |
| 8.20% notes, due August 2011, net of unamortized discount of \$501 and \$536 <sup>(b)</sup>   | 249,499                   | 249,464                           |
| 7.25% notes, due August 2005, net of unamortized discount of \$18 and \$25 <sup>(c)</sup>   | 99,982                    | 99,975                            |
| Asset securitization facility <sup>(d)</sup>  |                           | 9,000                             |
| Industrial revenue bonds, bearing interest at variable rates (2.47% at March 31, 2004 and 2.54% at September 30, 2003), due through October 2036 <sup>(e)</sup> | 37,400                    | 37,400                            |
| Revolving credit facility <sup>(f)</sup>  |                           | 3,500                             |
| Other notes   | 2,666                     | 2,863                             |
|   | <hr/>                     | <hr/>                             |
|   | 489,321                   | 501,964                           |
| Less current maturities of debt   | 414                       | 12,927                            |
|   | <hr/>                     | <hr/>                             |
| Long-term debt due after one year   | \$488,907                 | \$ 489,037                        |
|   | <hr/>                     | <hr/>                             |

<sup>(a)</sup> In March 2003, we sold \$100.0 million in aggregate principal amount of our 5.625% notes due March 15, 2013 (which we refer to as the **2013 Notes**). The 2013 Notes are not redeemable prior to maturity and are not subject to any sinking fund requirements. The 2013 Notes are unsubordinated, unsecured obligations. The indenture related to the 2013 Notes restricts us and our subsidiaries from incurring certain liens and entering into certain sale and leaseback transactions, subject to a number of exceptions. Debt issuance costs of approximately \$0.8 million are being amortized over the term of the 2013 Notes. Giving effect to the amortization of the original issue discount, and the debt issuance costs, the effective interest rate on the 2013 Notes is approximately 5.744%.

<sup>(b)</sup> In August 2001, we sold \$250.0 million in aggregate principal amount of our 8.20% notes due August 15, 2011 (which we refer to as the **2011 Notes**). The 2011 Notes are not redeemable prior to maturity and are not subject to any sinking fund requirements. The 2011 Notes are unsubordinated, unsecured obligations. The indenture related to the 2011 Notes restricts us and our subsidiaries from incurring certain liens and entering into certain sale and leaseback transactions, subject to a number of exceptions. The 2011 Notes were issued at a discount of

\$0.7 million, which is being amortized over the term of the 2011 Notes. Debt issuance costs of approximately \$2.1 million are being amortized over the term of the 2011 Notes. Giving effect to the amortization of the original issue discount and the debt issuance costs, the effective interest rate of the 2011 Notes is approximately 8.31%.

- (c) In August 1995, we sold \$100.0 million in aggregate principal amount of our 7.25% notes due August 1, 2005 (which we refer to as the **2005 Notes**). The 2005 Notes are not redeemable prior to maturity and are not subject to any sinking fund requirements. The 2005 Notes are unsubordinated, unsecured obligations. The indenture related to the 2005 Notes restricts us and our subsidiaries from incurring certain liens and entering into certain sale and leaseback transactions, subject to a number of exceptions. Debt issuance costs of approximately \$0.9 million are being amortized over the term of the 2005 Notes. In May 1995, we entered into an interest rate adjustment transaction in order to effectively fix the interest rate on the 2005 Notes subsequently issued in August 1995. The costs associated with the interest rate adjustment transaction of \$1.5 million are being amortized over the term of the 2005 Notes. Giving effect to the amortization of the original issue discount, the debt issuance costs and the costs associated with the interest rate adjustment transaction, the effective interest rate on the 2005 Notes is approximately 7.51%. In April 2004, we purchased \$11.0 million of our 2005 Notes at a price of 106.1% of par value. See Note 14 Subsequent Events.

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- (d) In November 2000, we entered into a \$125.0 million receivables-backed financing transaction (the **Receivables Financing Facility**). A bank provides a back-up liquidity facility. We had no outstanding borrowing under this facility as of March 31, 2004. The effective interest rate, which consists of an average commercial paper rate for the period and a fee for the used and unused portion of the facility, was 2.10% as of September 30, 2003. Both the Receivables Financing Facility and the back-up liquidity facility are 364-day vehicles. Our Receivables Financing Facility was scheduled to expire on March 29, 2004. We extended the facility until April 29, 2004. On April 29, 2004, we renewed the facility through March 28, 2005, and reduced the size of the facility from \$125.0 million to \$75.0 million.
- (e) Payments of principal and interest on these industrial revenue bonds are guaranteed by a letter of credit issued by a bank. Restrictive covenants similar to those described in note (f) below exist under the terms of the letter of credit agreements. The bonds are remarketed periodically based on the interest rate period selected by us. In the event the bonds cannot be remarketed, the bank has agreed to extend long-term financing to us in an amount sufficient to retire the bonds. The bonds are secured by the underlying assets.
- (f) In March 2003, we amended our revolving credit facility, provided by a syndicate of banks, to reduce the size of the facility from \$300.0 million to \$125.0 million through June 2005. Combined credit availability under the Receivables Financing Facility and the revolving credit facility exceeds \$100.0 million as of March 31, 2004. Borrowings outstanding under the revolving credit facility bear interest based upon LIBOR plus an applicable margin. Annual facility fees range from 0.125% to 0.50% of the aggregate borrowing availability, based on the ratio of our consolidated funded debt to a financial measure referred to as EBITDA in the documentation for our revolving credit facility (which we refer to as "**Credit Facility Earnings Before Special Items**"). Credit Facility Earnings Before Special Items is not a defined term under accounting principles generally accepted in the United States and should not be considered as an alternative financial measure to cash flows from operations as a measure of liquidity or to net income as a measure of operating results. This liquidity measure, which is referred to as EBITDA in our revolving credit facility, differs from the term EBITDA as the SEC defines the term for disclosure purposes, which is earnings (net income) before interest expense, taxes (income tax expense), depreciation, and amortization. The borrowing rate, and facility fee, at March 31, 2004 was 2.25% and 0.25% respectively. The borrowing rate and facility fee at September 30, 2003 were 2.25% and 0.25%, respectively. The agreements covering this facility include restrictive covenants regarding the maintenance of financial ratios, creation of additional long-term and short-term debt, certain leasing arrangements, mergers, acquisitions, disposals and other matters. We are in compliance with such restrictions. On May 3, 2004, we reduced the size of our Revolving Credit Facility from \$125.0 million to \$75.0 million. See Note 14 Subsequent Events.

**Note 12. Retirement Plans**

The following table represents a summary of the components of net pension cost for the three and six months ended March 31, 2004 and March 31, 2003 (in thousands):

|                                    | <b>Three Months Ended</b> |                  | <b>Six Months Ended</b> |                  |
|------------------------------------|---------------------------|------------------|-------------------------|------------------|
|                                    | <b>March 31,</b>          | <b>March 31,</b> | <b>March 31,</b>        | <b>March 31,</b> |
|                                    | <b>2004</b>               | <b>2003</b>      | <b>2004</b>             | <b>2003</b>      |
| Service cost                       | \$ 2,298                  | \$ 1,814         | \$ 4,557                | \$ 3,710         |
| Interest cost                      | 4,333                     | 4,031            | 8,666                   | 8,062            |
| Expected return on plan assets     | (4,087)                   | (4,056)          | (8,173)                 | (7,753)          |
| Amortization of prior service cost | 12                        | 13               | 23                      | 25               |
| Amortization of net loss           | 1,632                     | 703              | 3,264                   | 1,406            |

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|  |          |          |          |          |
|--|----------|----------|----------|----------|
| Pension curtailment                                      | 100      | _____    | 100      | _____    |
| Company defined benefit plan expense                     | 4,288    | 2,505    | 8,437    | 5,450    |
| Multi-employer plans for collective bargaining employees | 129      | 103      | 246      | 204      |
|  | _____    | _____    | _____    | _____    |
| Net pension cost   | \$ 4,417 | \$ 2,608 | \$ 8,683 | \$ 5,654 |
|  | _____    | _____    | _____    | _____    |

We expect to contribute \$19.5 million to our pension plans in fiscal 2004 in order to maintain a 90% funded level. The current year net pension cost reflected in the table above assumes the payment will be made. As of March 31, 2004 we have contributed approximately \$0.1 million.

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**Note 13. Commitments and Contingencies**

***Environmental and Other Matters***

We are subject to various federal, state, local and foreign environmental laws and regulations, including those regulating the discharge, storage, handling and disposal of a variety of substances. These laws and regulations include, among others, the Comprehensive Environmental Response, Compensation and Liability Act ( **CERCLA** ), the Clean Air Act (as amended in 1990), the Clean Water Act, the Resource Conservation and Recovery Act (including amendments relating to underground tanks) and the Toxic Substances Control Act. These environmental regulatory programs are primarily administered by the U.S. Environmental Protection Agency ( **US EPA** ). In addition, some states in which we operate have adopted equivalent or more stringent environmental laws and regulations or have enacted their own parallel environmental programs, which are enforced through various state administrative agencies.

We do not believe that future compliance with these environmental laws and regulations will have a material adverse effect on our results of operations, financial condition or cash flows. However, environmental laws and regulations are becoming increasingly stringent. Consequently, our compliance and remediation costs could increase materially. In addition, we cannot currently assess with certainty the impact that the future emissions standards and enforcement practices associated with changes to regulations promulgated under the Clean Air Act will have on our operations or capital expenditure requirements. However, we believe that any such impact or capital expenditures will not have a material adverse effect on our results of operations, financial condition or cash flows.

We account for environmental related costs as follows:

We accrue for losses associated with our environmental remediation obligations when both of the following are true: it is probable that we have incurred a liability and the amount of the loss can be reasonably estimated.

We generally recognize accruals for estimated losses from our environmental remediation obligations no later than completion of the remedial feasibility study.

We adjust such accruals as further information develops or circumstances change.

We recognize recoveries of our environmental remediation costs from other parties as assets when their receipt is deemed probable.

We have been identified as a potentially responsible party ( **PRP** ) at nine active superfund sites pursuant to CERCLA or comparable state statutes ( **Superfund legislation** ). Based upon currently available information and the opinions of our environmental compliance managers and general counsel, although there can be no assurance, we have reached the following conclusions with respect to these nine sites:

With respect to each of two sites, while we have been identified as a PRP, our records indicate that we have no evidence that we are associated with the site. Accordingly, if we are considered to be a PRP, we believe that we should be categorized as an unproven PRP.

With respect to each of seven sites, we preliminarily determined that it is probable that we had incurred a liability with respect to the site and that one of the following conclusions was applicable:

With respect to each of five sites, we determined that it was appropriate to conclude that, while it was not estimable, the potential liability was reasonably likely to be a *de minimus* amount. With respect to each of these sites, we also believe that any reasonably likely exposure to liability will be *de minimus* and immaterial.

With respect to each of two sites, while we have preliminarily determined that we may be associated with the site, we also determined that it was appropriate to conclude that the potential liability was best reflected by a range of reasonably possible liabilities all of which we expect to be *de minimus* and immaterial.

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***Seven Hills Arbitration***

The Company and Lafarge have agreed to enter into arbitration with respect to the price of gypsum plasterboard liner that Seven Hills is entitled to charge Lafarge from November 2002 going forward. The arbitration will also determine certain amounts that the Company is entitled to recover from Seven Hills for certain services rendered to Seven Hills by the Company. The arbitration is expected to commence during the third fiscal quarter. While we are unable to predict with certainty the outcome of the arbitration, management believes that it is unlikely that the final determination will materially affect the financial results of the Company.

**Note 14. Subsequent Events**

In April 2004, we purchased \$11.0 million of our 2005 Notes at a price of 106.1% of par value. Concurrently, we terminated \$11.0 million of our interest rate swap on our 2005 Notes. The premium paid over par for the debt less the favorable impact of unamortized realized interest rate swap gains resulted in an overall net loss of \$0.3 million to the Company. This loss will be reflected in our results of operations for the third quarter of fiscal 2004.

Our Receivables Financing Facility was scheduled to expire on March 29, 2004. We extended the facility until April 29, 2004. On April 29, 2004, we renewed the facility through March 28, 2005, and reduced the size of the facility from \$125.0 million to \$75.0 million. On May 3, 2004, we reduced the size of our revolving credit facility from \$125.0 million to \$75.0 million.

Our combined credit availability under the Receivables Financing Facility and the revolving credit facility exceeded \$100.0 million as of March 31, 2004.



**Table of Contents****Note 15. Segment Information**

The following table shows certain operating data for our three industry segments (in thousands). Certain of our income and expenses are not allocated to our segments and are thus not reflected in the information used by management to make operating decisions and assess performance. These items are reported as non-allocated expenses. These items include elimination of intercompany profit, restructuring and other costs and certain corporate expenses.

|   | <b>Three Months Ended</b> | <b>Three Months Ended</b> | <b>Six Months Ended</b> | <b>Six Months Ended</b> |
|---|---------------------------|---------------------------|-------------------------|-------------------------|
|   | <b>March 31,</b>          | <b>March 31,</b>          | <b>March 31,</b>        | <b>March 31,</b>        |
|   | <b>2004</b>               | <b>2003</b>               | <b>2004</b>             | <b>2003</b>             |
| Net sales (aggregate):                          |                           |                           |                         |                         |
| Packaging Products                              | \$231,772                 | \$196,277                 | \$440,647               | \$369,954               |
| Merchandising Displays and Corrugated Packaging | 75,725                    | 64,214                    | 147,995                 | 137,924                 |
| Paperboard                                      | 137,843                   | 130,742                   | 267,372                 | 253,878                 |
|   | <u>445,340</u>            | <u>391,233</u>            | <u>856,014</u>          | <u>761,756</u>          |
| Total   |                           |                           |                         |                         |
| Less net sales (intersegment):                  |                           |                           |                         |                         |
| Packaging Products                              | 908                       | 881                       | 1,874                   | 1,580                   |
| Merchandising Displays and Corrugated Packaging | 1,176                     | 1,115                     | 2,274                   | 2,350                   |
| Paperboard                                      | 43,256                    | 39,003                    | 85,756                  | 77,743                  |
|   | <u>45,340</u>             | <u>40,999</u>             | <u>89,904</u>           | <u>81,673</u>           |
| Total   |                           |                           |                         |                         |
| Net sales (unaffiliated customers):             |                           |                           |                         |                         |
| Packaging Products                              | 230,864                   | 195,396                   | 438,773                 | 368,374                 |
| Merchandising Displays and Corrugated Packaging | 74,549                    | 63,099                    | 145,721                 | 135,574                 |
| Paperboard                                      | 94,587                    | 91,739                    | 181,616                 | 176,135                 |
|   | <u>\$400,000</u>          | <u>\$350,234</u>          | <u>\$766,110</u>        | <u>\$680,083</u>        |
| Total   |                           |                           |                         |                         |
| Segment income:                                 |                           |                           |                         |                         |
| Packaging Products                              | \$ 9,894                  | \$ 9,742                  | \$ 16,625               | \$ 14,396               |
| Merchandising Displays and Corrugated Packaging | 7,161                     | 5,073                     | 12,859                  | 11,980                  |
| Paperboard                                      | 2,582                     | 6,351                     | 5,398                   | 11,412                  |
|   | <u>\$ 19,637</u>          | <u>\$ 21,166</u>          | <u>\$ 34,882</u>        | <u>\$ 37,788</u>        |

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|  |                   |                   |                   |                   |
|--|-------------------|-------------------|-------------------|-------------------|
| Total segment income                                   | 19,637            | 21,166            | 34,882            | 37,788            |
| Restructuring and other costs                          | (6,043)           | (935)             | (6,175)           | (416)             |
| Other non-allocated expenses                           | (2,408)           | (1,278)           | (3,926)           | (2,993)           |
| Interest expense                                       | (5,871)           | (6,566)           | (11,782)          | (13,029)          |
| Interest and other income                              | 132               | 56                | 212               | 108               |
| Minority interest in income of consolidated subsidiary | (590)             | (784)             | (1,476)           | (1,522)           |
|  | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u> |
| Income from continuing operations before income taxes  | \$ 4,857          | \$ 11,659         | \$ 11,735         | \$ 19,936         |
|  | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u> |

Table of Contents**PART I. FINANCIAL INFORMATION****Item 2. *MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS***

The following discussion should be read in conjunction with the condensed consolidated financial statements and notes thereto, included herein, and our audited consolidated financial statements and notes thereto for the fiscal year ended September 30, 2003, as well as the information under the heading "*Management's Discussion and Analysis of Financial Condition and Results of Operations*," that are part of our Fiscal 2003 Form 10-K which we filed with the SEC on December 19, 2003. The table in Note 15 to the condensed consolidated financial statements shows certain operating data for our three industry segments.

**Overview**

The trends in sales volume for most of our major businesses were positive in the second quarter of fiscal 2004 compared to the same period last year. Net sales increased in each of our segments for the three and six months ended March 31, 2004 despite a pricing environment for our products that remains highly competitive. Folding carton division sales increased due to growth in our business that was not attributable to acquisitions during the period (which we refer to as our **base business**) and growth arising from our acquisitions completed during fiscal 2003. Net sales of merchandising displays increased primarily due to strong demand and sales to new customers as we expanded our presence in the North American display business. We expect display sales to be weaker in the coming quarter as we begin to experience the complete impact of transitioning out the business of the customers whose business we previously reported we had lost due to competitive bidding. While we began to experience the transitioning in of new business we were awarded during fiscal 2003, we did not experience as much of the transitioning out of lost business during the second quarter of fiscal 2004 as we had previously anticipated. The market for merchandising displays continues to reflect price competitiveness through more frequent bidding for business and increased demand for lower cost displays with more economical designs. Our corrugated packaging division net sales increased in the second quarter of fiscal 2004, but continued to experience pricing pressure for its products. Net sales in our interior packaging division decreased slightly on lower volume and pricing. We expect net sales to show a modest gain in the fourth fiscal quarter as we transition in a new customer. Our Paperboard Segment net sales have increased as a result of higher selling prices and increased volumes. We announced board price increases that seek to recover higher costs such as fiber, energy, chemicals, and pension expense. The price increases will begin to take effect in April 2004. We expect these price increases will begin to contribute to revenue in the third quarter of fiscal 2004 and have a greater impact in the fourth quarter of fiscal 2004. The price increase will be delayed, in part, because we sell a portion of our production on the basis of published index prices that do not immediately reflect such price increases. In March 2004, we announced the closure of our Wright City, Missouri laminated paperboard products facility. Sales by this facility in the first six months of fiscal 2004 and 2003 resulted in operating losses. We do not anticipate consolidating the majority of the sales of this operation into our remaining laminated facilities.

The increase in cost of goods sold as a percentage of sales we have experienced in fiscal 2004 resulted primarily from increases in fiber and energy costs at our recycled paperboard mills. The energy costs continue to be driven by higher natural gas prices.

In fiscal 2004, we have experienced increased pension expense compared to the prior year. We expect our annual pension cost will increase from approximately \$11 million in fiscal 2003 to approximately \$17 million in fiscal 2004. Assuming we continue to fund our pensions at the 90% level, and, assuming our assumptions for the discount rate, increase in compensation levels, and long term rate of return on plan assets remain as disclosed in our Fiscal 2003 Form 10-K, we expect pension expense to decrease to approximately \$15 million in fiscal 2005.

**Critical Accounting Policies**

Our accompanying condensed consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States, which require management to make estimates and assumptions that affect the amounts of revenues, expenses, assets and liabilities reported. The disclosure under the caption

*Management's Discussion and Analysis of Financial Condition and Results of Operations - Critical Accounting Policies* in our Fiscal 2003 Form 10-K is a discussion of certain critical accounting matters that are

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important to the portrayal of our financial condition and results of operations and that require some of management's most subjective and complex judgments. The accounting for these matters involves the making of estimates and assumptions based on current facts and circumstances that, in management's judgment, are material due to the levels of subjectivity and judgment necessary to account for highly uncertain matters or the susceptibility of such matters to change. In management's judgment, the impact of these estimates and assumptions on our reported financial condition and results of operations is also material and may cause our actual financial condition and results of operations to differ materially. Set forth below, is disclosure that supplements and updates certain aspects of the critical accounting policies disclosure in the Fiscal 2003 Form 10-K:

***Impairment of Long-Lived Assets and Goodwill***

We account for our goodwill under Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets* ( **SFAS 142** ). We review the recorded value of our goodwill annually at the beginning of the fourth quarter of each fiscal year, or sooner if events or changes in circumstances indicate that the carrying amount may exceed fair value. We determine recoverability by comparing the estimated fair value of the reporting unit to which the goodwill applies to the carrying value, including goodwill, of that reporting unit.

The SFAS 142 goodwill impairment model is a two-step process. In step 1, we utilize the present value of expected net cash flows to determine the estimated fair value of our reporting units. This present value model requires management to estimate future net cash flows, the timing of these cash flows, and a discount rate (based on our weighted average cost of capital), which represents the time value of money and the inherent risk and uncertainty of the future cash flows. The assumptions we use to estimate future cash flows are consistent with the assumptions that the reporting units use for internal planning purposes. If we determine that the estimated fair value of the reporting unit exceeds its carrying amount, goodwill of the reporting unit is not impaired. If we determine that the carrying amount of the reporting unit exceeds its estimated fair value, we must complete step 2 of the impairment analysis. Step 2 involves determining the implied fair value of the reporting unit's goodwill and comparing it to the carrying amount of that goodwill. If the carrying amount of the reporting unit's goodwill exceeds the implied fair value of that goodwill, we recognize an impairment loss in an amount equal to that excess.

Our judgments regarding the existence of impairment indicators are based on legal factors, market conditions and operational performance. Future events could cause us to conclude that impairment indicators exist and that assets associated with a particular operation are impaired. Evaluating the impairment also requires us to estimate future operating results and cash flows, which also require judgment by management. Any resulting impairment loss could have a material adverse impact on our financial condition and results of operations.

In connection with the shutdown of our facility in Wright City, Missouri, we recorded a goodwill impairment charge of \$0.2 million for the Wright City facility. Subsequently, we performed step 1 of the SFAS 142 impairment test for the Laminated Paperboard Products division. The results of our testing indicated the goodwill of the Laminated Paperboard Products division was not further impaired.

We follow SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* ( **SFAS 144** ), in determining whether the carrying value of any of our long-lived assets is impaired. The SFAS 144 test is a 3-step test for assets that are held and used as that term is defined by SFAS 144. First, we determine whether indicators of impairment are present. SFAS 144 requires us to review long-lived assets for impairment only when events or changes in circumstances indicate that the carrying amount of the long-lived asset might not be recoverable. Accordingly, while we do routinely assess whether impairment indicators are present, we do not routinely perform tests of recoverability. Second, we determine whether the estimated undiscounted cash flows for the potentially impaired assets are less than the carrying value. This model requires management to estimate future net cash flows. The assumptions we use to estimate future cash flows are consistent with the assumptions we use for internal planning

purposes, updated to reflect current expectations. Third, we estimate the fair value of the asset and record an impairment charge if the carrying value is less than the fair value of the asset. The test is similar for assets classified as held for sale, except that the assets are recorded at the lower of their carrying value or fair value less anticipated cost to sell.

Our judgments regarding the existence of impairment indicators are based on legal factors, market conditions and operational performance. Future events could cause us to conclude that impairment indicators exist and that assets associated with a particular operation are impaired. Evaluating the impairment also requires us to estimate future operating results and cash flows, which also require judgment by management. Any resulting impairment loss could have a material adverse impact on our financial condition and results of operations.

**Table of Contents*****Self-Insurance***

We are self-insured for the majority of our group health insurance costs, subject to specific retention levels. We calculate our group insurance reserve based on a combination of claims lag data provided by our claims administrators and, if claims lag data is not available, we use estimated rates provided by our insurance consultants. At the end of each month during a fiscal year, we calculate our average monthly claims paid utilizing the actual monthly payments during the trailing 12-month period. At that time, we also calculate our required reserve utilizing payment lag information during that 12-month period. For example, during the last 12-month period, the average monthly claims paid fluctuated between \$2.4 million and \$2.5 million and our average claims lag fluctuated between 1.43 and 1.52 times the average monthly claims paid. Our accrual at March 31, 2004 represents approximately 1.52 times the average monthly claims paid. A 5% change in the average claims lag would change our reserve by approximately \$0.2 million. While we believe that our assumptions are appropriate, significant differences in our actual experience or significant changes in our assumptions may materially affect our group health insurance costs.

***Accounting for Income Taxes***

As part of the process of preparing our consolidated financial statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate. We estimate our actual current tax exposure and assess temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our consolidated balance sheet. A 1% increase in our effective tax rate would increase tax expense by approximately \$0.1 million for the six months ended March 31, 2004. While we believe that our assumptions are appropriate, significant differences in our actual experience or significant changes in our assumptions may materially affect our income tax exposure.

***Pension and Other Post-Retirement Benefits***

The determination of our obligation and expense for pension and other post-retirement benefits is dependent on our selection of certain assumptions used by actuaries in calculating such amounts. Those assumptions are described in Note 11 to the consolidated financial statements in our Fiscal 2003 Form 10-K and include, among others, the discount rate, expected long-term rate of return on plan assets and rates of increase in compensation levels. During fiscal 2003, the effect of a 0.25% change in the discount rate would have impacted income before income taxes by approximately \$1.0 million. During fiscal 2003, the effect of a 0.25% change in the expected long-term rate of return on plan assets would have impacted income before income taxes by approximately \$0.5 million.

In accordance with accounting principles generally accepted in the United States, actual results that differ from our assumptions are accumulated and amortized over future periods and, therefore, generally affect our recognized expense, recorded obligation and funding requirements in future periods. While we believe that our assumptions are appropriate, significant differences in our actual experience or significant changes in our assumptions may materially affect our pension and other post-retirement benefit obligations and our future expense.

**Results of Operations (Consolidated)*****Net Sales (Unaffiliated Customers)***

| <b>(\$ In Millions)</b> | <b>First<br/>Quarter</b> | <b>Second<br/>Quarter</b> | <b>Six<br/>Months<br/>Ended<br/>3/31</b> | <b>Third<br/>Quarter</b> | <b>Fourth<br/>Quarter</b> | <b>Fiscal<br/>Year</b> |
|-------------------------|--------------------------|---------------------------|--|--------------------------|---------------------------|------------------------|
|                         |                          |                           |  |                          |                           |                        |

|                 |                |                |                |         |         |           |
|-----------------|----------------|----------------|----------------|---------|---------|-----------|
| 2003            | \$329.8        | \$350.3        | \$680.1        | \$368.2 | \$385.0 | \$1,433.3 |
| <b>2004</b>     | <b>\$366.1</b> | <b>\$400.0</b> | <b>\$766.1</b> |         |         |           |
| <b>% Change</b> | <b>11.0%</b>   | <b>14.2%</b>   | <b>12.6%</b>   |         |         |           |

The increase in net sales for the quarter ended March 31, 2004 compared to the prior year quarter was primarily due to strong net sales increases in our folding carton and merchandising display businesses. Our paperboard segment also experienced increased net sales.



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The increase in net sales for the six months ended March 31, 2004 compared to the prior year period was primarily due to strong net sales increases in our folding carton, merchandising display, and paperboard businesses.

We have provided further information regarding factors that impacted net sales in the segment discussions included below under the heading *Results of Operations (Segment Data)*.

**Cost of Goods Sold**

| (\$ In Millions) | First<br>Quarter | Second<br>Quarter | Six<br>Months<br>Ended<br>3/31 | Third<br>Quarter | Fourth<br>Quarter | Fiscal<br>Year |
|------------------|------------------|-------------------|--------------------------------|------------------|-------------------|----------------|
| 2003             | \$267.9          | \$287.1           | \$555.0                        | \$299.8          | \$313.5           | \$1,168.3      |
| (% of Net Sales) | 81.2%            | 82.0%             | 81.6%                          | 81.4%            | 81.4%             | 81.5%          |
| <b>2004</b>      | <b>\$304.3</b>   | <b>\$331.6</b>    | <b>\$635.9</b>                 |                  |                   |                |
| (% of Net Sales) | <b>83.1%</b>     | <b>82.9%</b>      | <b>83.0%</b>                   |                  |                   |                |

The increase in cost of goods sold as a percentage of sales for the quarter ended March 31, 2004 compared to the prior year quarter resulted primarily from increased fiber and energy costs at our recycled paperboard mills amounting to \$4.6 million (1.1% of net sales) and \$3.8 million (0.9% of net sales), respectively. The energy costs continue to be driven by higher natural gas prices. We also experienced increased pension expense of \$1.3 million (0.3% of net sales) compared to the prior year quarter.

The increase in cost of goods sold as a percentage of sales for the six months ended March 31, 2004 compared to the same period last year resulted primarily from increased fiber and energy costs at our recycled paperboard mills amounting to \$5.7 million (0.7% of net sales) and \$6.4 million (0.8% of net sales), respectively. The energy costs continue to be driven by higher natural gas prices. In fiscal 2003, we hedged most of our winter requirements for natural gas purchases at a NYMEX equivalent price of less than \$3.50 per MMBtu (million British thermal units). In fiscal 2004, we hedged approximately two-thirds of our winter energy purchases at a NYMEX equivalent price of approximately \$5.20 per MMBtu that resulted in a small benefit compared to the winter spot prices. We also experienced increased pension expense of \$2.3 million (0.3% of net sales) during the six-month period compared to the prior year period. We have provided further information regarding factors that impacted cost of goods sold in the segment discussions included below under the heading *Results of Operations (Segment Data)*.

Substantially all of our U.S. inventories are valued at the lower of cost or market with cost determined on the last-in, first-out (LIFO) inventory valuation method, which we believe generally results in a better matching of current costs and revenues than under the first-in, first-out (FIFO) inventory valuation method. In periods of decreasing costs, the LIFO method generally results in lower cost of goods sold than under the FIFO method. In periods of increasing costs, the results are generally the opposite. Our quarterly results of operations reflect LIFO estimates based on management's projection of expected year-end inventory levels and costs.

The following table illustrates the comparative effect of LIFO and FIFO accounting on our results of operations. These supplemental FIFO earnings reflect the after-tax effect of eliminating the LIFO adjustment each year.

| Three months ended March 31,<br>2004 | 2003 | Six months ended March 31,<br>2004 | 2003 |
|--------------------------------------|------|------------------------------------|------|
|--------------------------------------|------|------------------------------------|------|

| (In Millions)      | LIFO           | FIFO           | LIFO    | FIFO    | LIFO           | FIFO           | LIFO    | FIFO    |
|--------------------|----------------|----------------|---------|---------|----------------|----------------|---------|---------|
| Cost of goods sold | <b>\$331.6</b> | <b>\$332.2</b> | \$287.1 | \$287.5 | <b>\$635.9</b> | <b>\$636.0</b> | \$555.0 | \$555.1 |
| Net income         | <b>2.9</b>     | <b>2.6</b>     | 7.3     | 7.1     | <b>14.8</b>    | <b>14.8</b>    | 12.4    | 12.3    |

**Table of Contents****Gross Profit**

|                  | First         | Second        | Six                     | Third   | Fourth  | Fiscal  |
|------------------|---------------|---------------|-------------------------|---------|---------|---------|
| (\$ In Millions) | Quarter       | Quarter       | Months<br>Ended<br>3/31 | Quarter | Quarter | Year    |
| 2003             | \$61.9        | \$63.2        | \$125.1                 | \$68.4  | \$71.6  | \$265.1 |
| (% of Net Sales) | 18.8%         | 18.0%         | 18.4%                   | 18.6%   | 18.6%   | 18.5%   |
| <b>2004</b>      | <b>\$61.8</b> | <b>\$68.4</b> | <b>\$130.2</b>          |         |         |         |
| (% of Net Sales) | <b>16.9%</b>  | <b>17.1%</b>  | <b>17.0%</b>            |         |         |         |

For a discussion of factors that impacted our gross profit, see the discussion included above and below under the headings *Results of Operations (Consolidated) Net Sales (Unaffiliated Customers)*, *Results of Operations (Consolidated) Cost of Goods Sold* and *Results of Operations (Segment Data)*.

**Selling, General and Administrative Expenses**

|                  | First         | Second        | Six                     | Third   | Fourth  | Fiscal  |
|------------------|---------------|---------------|-------------------------|---------|---------|---------|
| (\$ In Millions) | Quarter       | Quarter       | Months<br>Ended<br>3/31 | Quarter | Quarter | Year    |
| 2003             | \$47.0        | \$43.0        | \$90.0                  | \$46.5  | \$48.1  | \$184.6 |
| (% of Net Sales) | 14.3%         | 12.3%         | 13.2%                   | 12.6%   | 12.5%   | 12.9%   |
| <b>2004</b>      | <b>\$48.0</b> | <b>\$51.1</b> | <b>\$99.1</b>           |         |         |         |
| (% of Net Sales) | <b>13.1%</b>  | <b>12.8%</b>  | <b>12.9%</b>            |         |         |         |

Selling, general and administrative ( **SG&A** ) expenses increased as a percentage of net sales in the quarter ended March 31, 2004 compared to the same quarter last year, primarily due to increased bad debt expense and increased commissions. Bad debt expense increased \$3.7 million (0.9% of net sales). We perform on-going evaluations of our customers' credit information, such as financial condition and payment history, and our bad debt expense can fluctuate based on customer credit quality and the size of our credit exposure to individual customers. In the second quarter of fiscal 2003, we lowered our allowance for bad debt by \$2.0 million, while in the same period this year we incurred expense of \$1.7 million. Commissions expense increased \$1.0 million (0.3% of net sales) in the second quarter of fiscal 2004 compared to the same quarter last year. The increase in commissions was driven by increased sales, primarily in our folding carton business.

SG&A expenses decreased as a percentage of net sales in the six months ended March 31, 2004 compared to the same period last year primarily due to the increase in net sales, which were up 12.6%. The reduction as a percentage of net sales was partially offset by increased bad debt expense and increased commissions. Bad debt expense increased \$3.4 million (0.4% of net sales) and commission expense increased \$1.6 million (0.2% of net sales) in the six months of fiscal 2004 compared to the same period last year. The increase in commissions was driven by increased sales, primarily in our folding carton business.

**Restructuring and Other Costs**

We recorded pre-tax restructuring and other costs of \$6.0 million and \$6.2 million for the second quarter of fiscal 2004 and the six months ended March 31, 2004, respectively. We recorded pre-tax charges of \$0.9 million and \$0.4 million for the second quarter of fiscal 2003 and the six months ended March 31, 2003, respectively. These charges are discussed below.

During the second quarter of fiscal 2004, we announced the closure of our Wright City, Missouri laminated paperboard facility effective March 31, 2004 and recorded a pre-tax charge of \$7.7 million. The charge consisted of an asset impairment charge of \$6.5 million to record the equipment and facility at their estimated fair value less cost to sell, a goodwill impairment charge of \$0.2 million, severance and other employee costs of \$0.4 million, inventory write-off of \$0.4 million, and other costs of \$0.2 million. The closure resulted in the termination of approximately 68 employees. Net sales at the facility for the six-month period ended March 31, 2004 and March 31, 2003 were \$5.1 million and \$6.7 million, respectively. Operating losses at the facility for the same six-month periods were \$1.6 million and \$1.9 million, respectively. We do not anticipate consolidating the majority of the sales of this operation into our other laminated facilities. Since the Wright City closure, we have streamlined the management of the operating facilities in the laminated paperboard products division. This new structure has reduced the costs associated with managing these facilities. Our Aurora, Illinois and Columbus, Indiana manufacturing facilities now

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operate as part of our mill division, and our Macon, Georgia manufacturing facility was transferred to our corrugated division. We expect to incur a charge of approximately \$0.6 million in severance and other employee costs related to these activities, most of which will be incurred in the third fiscal quarter of 2004. We also sold our previously closed Mundelein, Illinois merchandising display facility site for a pre-tax gain of \$1.8 million. In addition, we recorded a variety of charges from previously announced closures totaling \$0.1 million in the period.

During the six months ended March 31, 2004, we recorded a pre-tax charge of \$7.7 million for the closure of our Wright City facility, recorded a \$1.8 million pre-tax gain on the sale of our Mundelein facility, and incurred a variety of charges from previously announced closures totaling \$0.3 million. The charges from the previously announced closings consisted primarily of \$0.1 million for equipment relocation, \$0.1 million for inventory write-off, and \$0.1 million of carrying costs.

During the second quarter of fiscal 2003, we recorded a pre-tax charge of \$0.9 million. In that quarter, we announced the closure of our Hunt Valley, Maryland and Mundelein merchandising display facilities. The closures resulted in the termination of approximately 49 employees. In connection with these closings, we accrued \$0.1 million for severance and other employee costs. These facilities were consolidated into the operations of other existing facilities. The other \$0.8 million consisted primarily of the following: \$0.7 million for equipment relocation charges primarily consisting of \$0.3 million at our El Paso, Texas folding carton facility and \$0.3 million at our Vineland, New Jersey converting operation; \$0.2 million of inventory write-offs at our Dothan, Alabama corrugated facility; \$0.1 million for an accrual adjustment related to severance at our El Paso facility; a net gain of \$0.3 million for equipment sales primarily of folding carton equipment at our St. Paul, Minnesota folding carton facility; and miscellaneous other items at a variety of locations totaling \$0.1 million.

During the six months ended March 31, 2003, we recorded a pre-tax charge of \$0.4 million. The charge of \$0.4 million was net of a gain for accrual adjustments of \$1.0 million on previously announced facility closings. The \$1.0 million gain resulted from \$0.6 million in excess employee severance and other employee benefits due to employee voluntary terminations and working longer than planned in the notice period; and \$0.4 million in accrual reversals resulting from the earlier than planned sales of property associated with our facilities in Augusta, Georgia (\$0.1 million), Dothan, Alabama (\$0.1 million) and Vineland, New Jersey (\$0.2 million). Partially offsetting these accrual adjustments were \$1.2 million of equipment relocation expenses consisting primarily of \$0.7 million for Vineland, \$0.3 million for El Paso, and \$0.1 million for Dothan; \$0.2 million for an accrual adjustment for severance at our El Paso facility; \$0.1 million in severance adjustments for our Hunt Valley and Mundelein facilities; \$0.2 million of inventory write-offs at Dothan; a \$0.2 million net charge for the removal and ultimate sale of certain equipment in our St. Paul facility, a net gain on the sale of our Vineland property and equipment of \$0.5 million, and a charge of \$0.2 million for the loss on the sale of our Augusta property and equipment.

***Unconsolidated Joint Venture***

During the quarter ended March 31, 2004, our Seven Hills joint venture reported a loss of less than \$0.1 million compared to a \$0.3 million loss for the same quarter last year. The joint venture is structured so that our primary income is earned in fees paid by the joint venture to our mill division. The gains and losses that we recognize from the joint venture are calculated based upon how it performs versus benchmark performance standards that are set forth in the joint venture agreement.

During the six months ended March 31, 2004, our Seven Hills joint venture reported a loss of \$0.1 million compared to \$0.3 million loss for the same period last year.

The Company and Lafarge have agreed to enter into arbitration with respect to the price of gypsum plasterboard liner that Seven Hills is entitled to charge Lafarge from November 2002 going forward. The arbitration will also determine

certain amounts that the Company is entitled to recover from Seven Hills for certain services rendered to Seven Hills by the Company. The arbitration is expected to commence during the third fiscal quarter. While we are unable to predict with certainty the outcome of the arbitration, management believes that it is unlikely that the final determination will materially affect the financial results of the Company.

**Table of Contents*****Interest Expense***

Interest expense for the quarter ended March 31, 2004 decreased 10.6% to \$5.9 million from \$6.6 million for the quarter ended March 31, 2003. The decrease was primarily attributable to lower interest rates, resulting in decreased interest expense of \$0.6 million, and decreased expense of \$0.1 million due to a decrease in our average outstanding borrowings in the second quarter of fiscal 2004 compared to the same quarter last year. The decrease in rates was primarily due to our utilization of favorable interest rate swaps.

Interest expense for the six months ended March 31, 2004 decreased 9.6% to \$11.8 million from \$13.0 million for the six months ended March 31, 2003. The decrease was primarily attributable to lower interest rates, resulting in decreased interest expense of \$1.7 million, which was partially offset by increased expense of \$0.5 million due to an increase in our average outstanding borrowings in the first six months of fiscal 2004 compared to the same prior year period. The decrease in rates was primarily due to our utilization of favorable interest rate swaps.

***Provision for Income Taxes***

Income tax expense for the quarter ended March 31, 2004 was \$1.8 million compared to income tax expense of \$4.5 million for the quarter ended March 31, 2003. The Company's effective income tax rate decreased to 38.1% for the three months ended March 31, 2004 compared to 38.8% for the second quarter of fiscal 2003. The small change in rate was primarily the result of a shift in the proportion of total income taxable from the United States to foreign tax jurisdictions with lower rates. We estimate that the marginal effective income tax rate for our domestic operations for the quarter ended March 31, 2004 was approximately 38.25%.

Income tax expense for the six months ended March 31, 2004 was \$4.6 million compared to income tax expense of \$7.9 million for the same period last year. The Company's effective income tax rate decreased to 38.9% for the six months ended March 31, 2004 compared to 39.4% for the six months ended March 31, 2003. The small change in rate was primarily the result of a shift in the proportion of total income taxable from the United States to foreign tax jurisdictions with lower rates. We estimate that the marginal effective income tax rate for our domestic operations for the six months ended March 31, 2004 was approximately 38.25%.

***Discontinued Operations***

In the first quarter of fiscal 2004, we completed the sale of our plastic packaging division and the sale of some of the assets and liabilities that we acquired in the January 2003 Cartem Wilco acquisition that were associated with a small folding carton and label plant in Quebec. The plastic packaging division transaction closed effective October 27, 2003 and we received proceeds of approximately \$59.0 million. As a result of the transaction, we recorded an after-tax gain of approximately \$7.1 million. The sale of some of the Cartem Wilco assets and liabilities, effective December 1, 2003, resulted in no gain or loss and we received proceeds of approximately \$2.9 million. We expect to incur additional expenses totaling approximately \$0.2 million in the third and fourth quarter of fiscal 2004 primarily related to severance and other related employee costs for employees required to render future service as part of the plastic packaging division sale. We are expensing these costs ratably over the future service period, which is anticipated to expire in the fourth quarter of fiscal 2004. The plastic packaging sale transaction is subject to a final working capital adjustment, which we expect to complete in the third quarter of fiscal 2004. The adjustment is not expected to be material. We have reclassified the results of operations for these components as income from discontinued operations on the consolidated statements of operations for all periods presented.

We reported a loss from discontinued operations for the quarter ended March 31, 2004 of \$0.1 million compared to income of \$0.2 million for the quarter ended March 31, 2003. The charge in the second quarter of fiscal 2004 was primarily due to severance and other related employee costs, as noted above.

Income from discontinued operations for the six months ended March 31, 2004 was \$7.6 million compared to \$0.3 million for the six months ended March 31, 2003. Income from discontinued operations for the first six months of fiscal 2004 includes an after-tax gain of approximately \$7.1 million on the sale of our plastic packaging division.



**Table of Contents***Net Income*

| <b>(\$ In Millions)</b> | <b>First<br/>Quarter</b> | <b>Second<br/>Quarter</b> | <b>Six<br/>Months<br/>Ended<br/>3/31</b> | <b>Third<br/>Quarter</b> | <b>Fourth<br/>Quarter</b> | <b>Fiscal<br/>Year</b> |
|-------------------------|--------------------------|---------------------------|--|--------------------------|---------------------------|------------------------|
| 2003                    | \$ 5.1                   | \$ 7.3                    | \$ 12.4                                  | \$ 7.2                   | \$ 10.0                   | \$ 29.6                |
| <i>(% of Net Sales)</i> | 1.5%                     | 2.1%                      | 1.8%                                     | 2.0%                     | 2.6%                      | 2.1%                   |
| <b>2004</b>             | <b>\$ 11.9</b>           | <b>\$ 2.9</b>             | <b>\$ 14.8</b>                           |                          |                           |                        |
| <i>(% of Net Sales)</i> | <b>3.2%</b>              | <b>0.7%</b>               | <b>1.9%</b>                              |                          |                           |                        |

Net income in the second quarter of fiscal 2004 and 2003, respectively, included a loss of \$0.1 million and income of \$0.2 million from discontinued operations and pre-tax expense of \$6.0 million and \$0.9 million for restructuring and other costs. For a discussion of factors that impacted our restructuring and other costs, see the disclosure included under the headings *Results of Operations (Consolidated)* *Restructuring and Other Costs*.

Net income for the six months ended March 31, 2004 included income of \$7.6 million from discontinued operations and pre-tax expense of \$6.2 million for restructuring and other costs. Approximately \$7.1 million of the \$7.6 million of income from discontinued operations was due to the gain on the sale of the plastic packaging division. Net income for the six months ended March 31, 2003 included income of \$0.3 million from discontinued operations and pre-tax expense of \$0.4 million for restructuring and other costs. For a discussion of factors that impacted our restructuring and other costs, see the disclosure included under the headings *Results of Operations (Consolidated)* *Restructuring and Other Costs*.

*Earnings Per Common and Common Equivalent Share*

| <b>(\$ In Millions)</b> | <b>First<br/>Quarter</b> | <b>Second<br/>Quarter</b> | <b>Six<br/>Months<br/>Ended<br/>3/31</b> | <b>Third<br/>Quarter</b> | <b>Fourth<br/>Quarter</b> | <b>Fiscal<br/>Year</b> |
|-------------------------|--------------------------|---------------------------|--|--------------------------|---------------------------|------------------------|
| 2003                    | \$0.15                   | \$0.21                    | \$0.36                                   | \$0.21                   | \$0.28                    | \$0.85                 |
| <b>2004</b>             | <b>\$0.34</b>            | <b>\$0.08</b>             | <b>\$0.42</b>                            |                          |                           |                        |

For a discussion of factors that impacted our earnings per common and common equivalent dollars per share, see the disclosure included under the headings *Results of Operations (Consolidated)* *Net Income*.

**Results of Operations (Segment Data)***Packaging Products Segment (Aggregate before Intersegment Eliminations)*

| <b>(\$ In Millions)</b> | <b>Net Sales<br/>(Aggregate)</b> | <b>Operating<br/>Income</b> | <b>Return<br/>on<br/>Sales</b> |
|-------------------------|----------------------------------|-----------------------------|--------------------------------|
|                         |                                  |                             |                                |

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|                              |                   |                   |                   |
|------------------------------|-------------------|-------------------|-------------------|
| First Quarter                | \$173.7           | \$ 4.7            | 2.7%              |
| Second Quarter               | 196.3             | 9.7               | 5.0               |
|                              | <u>          </u> | <u>          </u> | <u>          </u> |
| Six Months Ended 3/31        | 370.0             | 14.4              | 3.9               |
| Third Quarter                | 210.1             | 10.5              | 5.0               |
| Fourth Quarter               | 221.3             | 12.7              | 5.7               |
|                              | <u>          </u> | <u>          </u> | <u>          </u> |
| Fiscal 2003                  | \$801.4           | \$ 37.6           | 4.7%              |
|                              | <u>          </u> | <u>          </u> | <u>          </u> |
| <b>First Quarter</b>         | <b>\$208.9</b>    | <b>\$ 6.7</b>     | <b>3.2%</b>       |
| <b>Second Quarter</b>        | <b>231.7</b>      | <b>9.9</b>        | <b>4.3</b>        |
|                              | <u>          </u> | <u>          </u> | <u>          </u> |
| <b>Six Months Ended 3/31</b> | <b>\$440.6</b>    | <b>\$ 16.6</b>    | <b>3.8%</b>       |
| <b>Third Quarter</b>         |                   |                   |                   |
| <b>Fourth Quarter</b>        |                   |                   |                   |
|                              | <u>          </u> | <u>          </u> | <u>          </u> |
| <b>Fiscal 2004</b>           |                   |                   |                   |
|                              | <u>          </u> | <u>          </u> | <u>          </u> |

**Table of Contents***Net Sales (Packaging Products Segment)*

The 18.1% increase in net sales for the packaging products segment for the quarter ended March 31, 2004 compared to the prior year quarter was primarily due to strong sales growth in our folding carton business where sales were up 22.2% from the prior year quarter. Approximately \$5.7 million of the \$35.5 million increase in segment sales is attributable to the Pacific Coast Packaging acquisition made in August 2003. Net sales in our interior packaging joint venture were down 2.7%, as a result of lower volume and lower prices.

The 19.1% increase in net sales for the packaging products segment for the six months ended March 31, 2004 compared to the same period last year was primarily due to strong sales growth in our folding carton business where sales were up 23.5% from the prior year period. Approximately \$29.3 million of the \$70.7 million increase in segment sales is attributable to the acquisitions made in fiscal 2003. Net sales in our interior packaging joint venture were down 1.4%, primarily on lower volume.

*Operating Income (Packaging Products Segment)*

Operating income attributable to the packaging products segment for the quarter ended March 31, 2004 increased 1.6% compared to the prior year quarter. The increase in operating income for the segment was primarily due to the increase in folding carton net sales. Operating income in our folding carton operations improved, but increased net sales were partially offset by the adverse impact on margins from continued pricing pressure. The increased sales were also partially offset by a \$2.0 million increase in bad debt expense due to a change in the credit quality of several customers in our folding carton division. Additionally, sales commissions and workers compensation expense in our folding carton operations increased by \$0.6 million and \$0.3 million, respectively. The increase in sales commissions was due to increased net sales. Operating income at our interior packaging joint venture decreased primarily due to increased workers compensation expense of \$0.2 million.

Operating income attributable to the packaging products segment for the six months ended March 31, 2004 increased 15.5% compared to the prior year quarter. The increase in operating income for the segment was primarily due to the increase in folding carton net sales. Operating income in our folding carton operations improved, but increased net sales were partially offset by the adverse impact on margins from continued pricing pressure. The increased sales were also partially offset by a \$1.6 million increase in bad debt expense due to a change in the credit quality of several customers and an inventory write-off of \$0.6 million due to a customer's bankruptcy. Additionally, sales commissions and workers compensation expense in our folding carton operations increased by \$1.1 million and \$0.7 million, respectively. The increase in sales commissions was due to increased net sales. Operating income at our interior packaging joint venture was relatively flat compared to the prior year period.

*Merchandising Displays and Corrugated Packaging Segment (Aggregate before Intersegment Eliminations)*

| <u>(\$ In Millions)</u> | <u>Net Sales<br/>(Aggregate)</u> | <u>Operating<br/>Income</u> | <u>Return<br/>on Sales</u> |
|-------------------------|----------------------------------|-----------------------------|----------------------------|
| First Quarter           | \$ 73.7                          | \$ 6.9                      | 9.4%                       |
| Second Quarter          | 64.2                             | 5.1                         | 7.9                        |
| Six Months Ended 3/31   | 137.9                            | 12.0                        | 8.7                        |
| Third Quarter           | 70.4                             | 6.7                         | 9.5                        |
| Fourth Quarter          | 76.8                             | 9.0                         | 11.8                       |

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|                              |                |               |             |
|------------------------------|----------------|---------------|-------------|
|                              | —              | —             | —           |
| Fiscal 2003                  | \$285.1        | \$27.7        | 9.7%        |
|                              | —              | —             | —           |
| <b>First Quarter</b>         | <b>\$ 72.3</b> | <b>\$ 5.7</b> | <b>7.9%</b> |
| <b>Second Quarter</b>        | <b>75.7</b>    | <b>7.2</b>    | <b>9.5</b>  |
|                              | —              | —             | —           |
| <b>Six Months Ended 3/31</b> | <b>\$148.0</b> | <b>\$12.9</b> | <b>8.7%</b> |
| <b>Third Quarter</b>         |                |               |             |
| <b>Fourth Quarter</b>        |                |               |             |
|                              | —              | —             | —           |
| <b>Fiscal 2004</b>           |                |               |             |
|                              | —              | —             | —           |

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*Net Sales (Merchandising Displays and Corrugated Packaging Segment)*

The 17.9% increase in net sales for the segment for the quarter ended March 31, 2004 compared to the prior year quarter resulted primarily from an increase in net sales of merchandising displays, which were up 20.7%. This increase occurred primarily due to strong demand and sales to new customers as we expanded our presence in the North American display business. Our corrugated packaging net sales increased 9.7% primarily due to higher volume that was partially offset by lower prices.

The 7.3% increase in net sales for the segment for the six months ended March 31, 2004 compared to the same period last year resulted primarily from an increase in net sales of merchandising displays, which were up 8.1%. This increase occurred primarily due to strong demand and sales to new customers as we expanded our presence in the North American display business. Our corrugated packaging net sales increased 4.8% primarily due to higher volume that was partially offset by lower prices.

*Operating Income (Merchandising Displays and Corrugated Packaging Segment)*

Operating income attributable to this segment for the quarter ended March 31, 2004 increased 41.2% compared to the prior year quarter. The increase in operating income for the quarter primarily resulted from our increased merchandising display sales as well as from increased corrugated packaging sales. Our SG&A expenses have increased in our merchandising displays division to support our increased sales levels. The primary factors causing the increase were increased salaries and other related employee costs of \$0.9 million and commissions of \$0.5 million. The impact of the increased sales was also partially offset by a \$0.9 million increase in bad debt expense due to the change in credit quality of several customers.

Operating income attributable to this segment for the six months ended March 31, 2004 increased 7.3% compared to the same period last year. The increase in operating income for the six-month period primarily resulted from our increased merchandising display sales as well as from increased corrugated packaging sales in the second quarter of fiscal 2004. Our SG&A expenses have increased in our merchandising displays division to support our increased sales levels. The primary factors causing the increase were increased salaries and other related employee costs of \$1.4 million and commissions of \$0.6 million. The impact of the increased sales was also partially offset by a \$0.6 million increase in bad debt expense due to the change in credit quality of several customers.

**Table of Contents****Paperboard Segment (Aggregate before Intersegment Eliminations)**

|                       | Net Sales<br>(In<br>Millions) | Operating<br>Income<br>(In<br>Millions) | Return<br>On<br>Sales | Coated<br>and<br>Specialty<br>Recycled<br>Paperboard<br>Tons<br>Shipped <sup>(a)</sup><br>(In<br>Thousands) | Average<br>Coated<br>and<br>Specialty<br>Recycled<br>Paperboard<br>Price <sup>(a)(b)</sup><br>(Per<br>Ton) | Corrugated<br>Medium<br>Tons<br>Shipped<br>(In<br>Thousands) | Average<br>Corrugated<br>Medium<br>Price <sup>(b)</sup><br>(Per<br>Ton) | Weighted<br>Average<br>Recovered<br>Paper<br>Cost <sup>(b)</sup><br>(Per<br>Ton) |
|-----------------------|-------------------------------|---|-----------------------|---|--|--|---|--|
| First Quarter         | \$ 123.1                      | \$ 5.1                                  | 4.1%                  | 217.3   | \$ 434   | 40.8   | \$ 343  | \$ 82  |
| Second Quarter        | 130.8                         | 6.3                                     | 4.9                   | 241.9   | 418  | 41.5   | 335   | 78   |
| Six Months Ended 3/31 | 253.9                         | 11.4                                    | 4.5                   | 459.2   | 426  | 82.3   | 339   | 80   |
| Third Quarter         | 130.3                         | 5.6                                     | 4.3                   | 239.3   | 437  | 40.4   | 340   | 88   |
| Fourth Quarter        | 131.9                         | 3.7                                     | 2.8                   | 234.6   | 438  | 45.0   | 333   | 86   |
| Fiscal 2003           | \$ 516.1                      | \$ 20.7                                 | 4.0%                  | 933.1   | \$ 432   | 167.7  | \$ 338  | \$ 83  |
| First Quarter         | \$ 129.5                      | \$ 2.8                                  | 2.2%                  | 230.7   | \$ 440   | 43.9   | \$ 331  | \$ 86  |
| Second Quarter        | 137.9                         | 2.6                                     | 1.9                   | 248.7   | 439  | 42.9   | 341   | 94   |
| Six Months Ended 3/31 | \$ 267.4                      | \$ 5.4                                  | 2.0%                  | 479.4   | \$ 439   | 86.8   | \$ 336  | \$ 90  |
| Third Quarter         |                               |   |                       |   |  |  |   |  |
| Fourth Quarter        |                               |   |                       |   |  |  |   |  |
| Fiscal 2004           |                               |   |                       |   |  |  |   |  |

(a) Recycled Paperboard Tons Shipped and Average Recycled Paperboard Price Per Ton include tons shipped by Seven Hills, our joint venture with Lafarge.

(b) The Average Recycled Paperboard and Corrugated Medium Prices represent the average gross sales price per manufactured ton shipped adjusted for volume discounts and freight billed or allowed. The Average Recycled Paperboard and Corrugated Medium Prices are not adjusted for payment discounts or sales returns and allowances. The Weighted Average Recovered Paper Cost represents the average cost of fiber per manufactured ton shipped, including related freight and brokerage costs.

*Net Sales (Paperboard Segment)*

The net sales increase of 5.4% for the segment in the second quarter of fiscal 2004 compared to the prior year quarter was primarily due to a 2.9% increase in paperboard tons shipped and an \$18 per ton increase in our average selling price for all tons shipped. Total tons shipped in the second quarter of fiscal 2004 for the paperboard segment increased to 291,685 tons from 283,364 tons shipped in the same quarter last year. Our recycled fiber division experienced an 18.8% increase in net sales driven by increased fiber prices and volume. Sales of laminated paperboard products continue to decline, as we continue to experience a decrease in demand for our products by customers in the ready-to-assemble furniture and book industries, which are our primary laminated paperboard products markets, as well as continued competitive pricing.

The net sales increase of 5.3% for the segment in the first six months of fiscal 2004 compared to the prior year period was primarily due to a 4.6% increase in paperboard tons shipped and an \$11 per ton increase in our average selling price for all tons shipped. Total tons shipped in the first six months of fiscal 2004 for the paperboard segment increased to 566,275 tons from 541,497 tons shipped in the same period last year. Our recycled fiber division experienced a 6.5% increase in net sales driven by increased fiber prices and volume. Sales of laminated paperboard products continue to decline for the reasons discussed above.

*Operating Income (Paperboard Segment)*

Operating income attributable to the paperboard segment for the quarter ended March 31, 2004 decreased 59.3% compared to the prior year quarter despite a 2.9% increase in paperboard tons shipped. Higher fiber costs (\$4.6 million or 1.1% of net sales) and energy costs (\$3.8 million or 0.9% of net sales) adjusted for the increased average selling price (\$5.2 million or 1.3% of net sales), negatively impacted the paperboard segment by \$3.1 million (0.8% of net sales) compared to the prior year quarter. The impact of increased sales in the segment was also partially offset by an increase in bad debt expense of \$0.7 million due to the change in credit quality of several customers. Operating income in our recycled fiber division increased 122.8% due primarily to increased fiber prices and volume, as described above. Operating income in our laminated paperboard division was slightly improved compared to the prior year quarter due primarily to reductions in SG&A expenses.

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Operating income attributable to the paperboard segment for the six months ended March 31, 2004 decreased 52.7% compared to the prior year period despite a 4.6% increase in paperboard tons shipped. Higher fiber costs (\$5.7 million or 0.7% of net sales) and energy costs (\$6.4 million or 0.8% of net sales) adjusted for the increased average selling price (\$6.0 million or 0.8% of net sales), negatively impacted the paperboard segment by \$6.1 million or 0.8% of net sales compared to the prior year quarter. The impact of increased sales in the segment was also partially offset by an increase in bad debt expense of \$1.2 million due to the change in credit quality of several customers. Operating income in our recycled fiber division decreased 11.7% primarily due to higher fiber costs, as described above.

**Liquidity and Capital Resources*****Working Capital and Capital Expenditures***

We fund our working capital requirements and capital expenditures from net cash provided by operating activities, borrowings under term notes, our Receivables Financing Facility and bank credit facilities, and proceeds received in connection with the issuance of industrial revenue bonds and debt and equity securities.

During the first quarter of fiscal 2004, we completed the sale of our plastic packaging division and the sale of some of the assets and liabilities associated with a small folding carton and label plant in Quebec that we acquired in the January 2003 Cartem Wilco acquisition. We received \$61.9 million in cash for the two transactions. The sale of our plastic packaging division is subject to a final working capital adjustment, which we expect to complete in our third fiscal quarter. The adjustment is not expected to be material.

Cash and cash equivalents were \$73.2 million at March 31, 2004, which increased from \$14.2 million at September 30, 2003. Net cash provided by operating activities decreased for the six months ended March 31, 2004 to \$35.1 million from \$51.6 million for the six months ended March 31, 2003. The decrease occurred in the first quarter of fiscal 2004. The decrease was primarily due to an increase in trade-related working capital from increases in accounts receivable, increases in inventory and decreases in accounts payable, as well as a decrease in accrued liabilities from the payment of employee bonuses. The fluctuations in accounts receivable and inventory are driven by increased sales. Net cash provided by investing activities was \$35.6 million for the six months ended March 31, 2004, which consisted primarily of \$59.0 million received for the sale of the plastic packaging division, and \$2.9 million for the sale of some of the Cartem Wilco assets and liabilities associated with a small folding carton and label plant in Quebec. Partially offsetting these asset sales proceeds were capital expenditures of \$30.3 million, and proceeds of \$5.2 million from the sale of property, plant and equipment. The proceeds from the sale of property, plant and equipment were primarily from the sale of our Mundelein, Illinois merchandising display facility site. Net cash used for investing activities for the six months ended March 31, 2003 was \$90.8 million and consisted primarily of capital expenditures of \$31.4 million, cash paid for the January 2003 purchase of Cartem Wilco of \$65.2 million, partially offset by \$5.2 million of proceeds from the sale of property, plant and equipment and \$1.5 million for the sale of our Montreal, Quebec recycled fiber collection facility. Proceeds from the sale of property, plant and equipment included asset sales proceeds of \$1.6 million from Vineland, New Jersey, \$1.3 million from Dothan, Alabama, \$0.9 million from Augusta, Georgia, and \$0.4 million from El Paso, Texas. Net cash used for financing activities aggregated \$12.1 million for the six months ended March 31, 2004 and consisted primarily of additions to and payments of other debt, proceeds from monetizing swap contracts, the issuance of common stock and cash dividends paid to shareholders. For the six months ended March 31, 2003, cash provided by financing activities aggregated \$38.5 million consisting primarily of additions to and payments of other debt, proceeds from monetizing swap contracts, the issuance of common stock and cash dividends paid to shareholders, and the issuance of \$100.0 million of 10-year notes maturing on March 15, 2013 which we used to pay down the balances on our revolving credit facility, our asset securitization facility and the debt that we incurred as part of the acquisition of Cartem Wilco.



At March 31, 2004, we had no outstanding balance under our \$125.0 million revolving credit facility compared to a \$3.5 million balance at September 30, 2003. In May 2004, we elected to reduce the size of this facility to \$75.0 million. The revolving credit facility terminates June 30, 2005. Our debt balance at March 31, 2004 was

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\$489.3 million compared to \$502.0 million on September 30, 2003, excluding the realized interest rate swap gains and the mark-to-market value of interest rate swaps totaling \$25.1 million and \$23.9 million, respectively. We estimate that our capital expenditures will aggregate approximately \$60 to \$67 million in fiscal 2004. We intend to use these expenditures for the purchase and upgrading of machinery and equipment, and for building expansions and improvements, including growth capital focused on our folding carton and merchandising display businesses. We believe that our financial position would support higher levels of capital expenditures, if justified by opportunities to increase revenues or reduce costs, and we continuously review new investment opportunities. Accordingly, it is possible that our capital expenditures in fiscal 2004 could be higher than currently anticipated.

We anticipate that we will be able to fund our capital expenditures, interest payments, stock repurchases, dividends and working capital needs for the foreseeable future from cash generated from operations, borrowings under our revolving credit facility and Receivables Financing Facility, proceeds from the issuance of debt or equity securities or other additional long-term debt financing.

## **New Accounting Standards**

See Note 2 of the condensed consolidated financial statements included herein for a full description of recent accounting pronouncements including the respective expected dates of adoption and expected effects on results of operations and financial condition.

## **Forward-Looking Statements**

Statements made in this report including statements regarding, among other things, our expectations regarding economic conditions, including the nature of the current market environment, the continuation of pricing pressures or the factors that affect such pressures, the impact of raw material and energy costs, the impact of announced price increases, the continuations of market trends, such as more frequent bidding for business, customer turnover and demand for lower cost products, as well as the impact and continuation of such factors; estimations regarding our results of operations, including expected costs and the continuation of cost trends, anticipated sales growth and the timing and impact of customer transitioning; the estimated impact of restructuring activities; the estimated amount and timing of severance and other related employee costs; the expected impact of post-closing working capital adjustments in acquisitions or dispositions; the estimated impact of ongoing litigation or other dispute resolutions; estimated capital expenditures for fiscal 2004; estimated marginal tax rate; the estimated impact of the gain and loss of customers; expectations regarding pension plan costs, funding requirements and earnings; and our ability to fund capital expenditures, interest payments, stock repurchases, dividends and working capital needs for the foreseeable future from available cash; expectations regarding environmental law liability as well as the expected impact of related compliance efforts; the impact of changes in assumptions and estimates underlying accounting policies; and the expected impact of implementing new accounting standards constitute forward-looking statements within the meaning of the Securities Act of 1933 and the Securities Exchange Act of 1934. Such statements are based on our current expectations and beliefs and are subject to certain risks and uncertainties that could cause actual amounts to differ materially from those projected in any forward looking statement. With respect to these forward-looking statements, we have made assumptions regarding, among other things, expected economic conditions; labor costs; the amount and timing of expected capital expenditures, including installation costs, project development and implementation costs, severance and other shutdown costs; restructuring costs; expected credit availability; expected volumes and price levels of purchases by customers; raw material and energy costs; expected year-end inventory levels and costs; and competitive conditions in our businesses. These forward-looking statements are subject to certain risks including, among others, that the foregoing assumptions are incorrect. There are many factors that impact these forward-looking statements that cannot be predicted accurately. Actual results may vary materially from current expectations, in part because we manufacture most of our products against customer orders with short lead times and small backlogs, while earnings are currently dependent on volume due to price levels and fixed operating costs.

Further, these forward-looking statements are subject to a number of general risks including, among others, decreases in demand for our products, increases in energy and raw material costs, reduced supplies of raw materials, increases in capital equipment costs, fluctuations in selling prices, adverse changes in general market and industry conditions, and possible adverse actions of our customers, our competitors and suppliers. Such risks are more particularly described in our filings with the SEC, including under the caption ***Business - Forward-looking Information and Risk Factors*** in our Fiscal 2003 Form 10-K. Management believes its estimates are reasonable; however, undue reliance should not be placed on such estimates, which are based on current expectations. Further, forward-looking statements speak only as of the date they are made, and we undertake no obligation to update any such information as future events unfold.

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

For a discussion of certain of the market risks to which we are exposed, see the *Quantitative and Qualitative Disclosures About Market Risk* section in our Fiscal 2003 Form 10-K.

**Interest Rates**

We are exposed to changes in interest rates, primarily as a result of our short-term and long-term debt. We use swap agreements to manage the interest rate characteristics of a portion of our outstanding debt. Based on the amounts and mix of fixed and floating rate debt at March 31, 2004 and September 30, 2003, if market interest rates increase an average of 100 basis points, after considering the effects of our swaps, our annual interest expense would increase by \$2.9 million and \$3.5 million, respectively. We determined these amounts by considering the impact of the hypothetical interest rate increase on our borrowing costs and interest rate swap agreements. These analyses do not consider the effects of changes in the level of overall economic activity that could exist in such an environment. Due to a change in our mix of fixed and floating rate debt at April 27, 2004, if market interest rates increase an average of 100 basis points, after considering the effects of our swaps, our annual interest expense would increase by \$3.8 million.

**Item 4. *CONTROLS AND PROCEDURES***

**Evaluation of Disclosure Controls and Procedures**

We maintain disclosure controls and other procedures that are designed with the objective of ensuring the following:

that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934 (the **Exchange Act**) is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms; and

that information required to be disclosed by us in the reports that we file under the Exchange Act is accumulated and communicated to our management, including our Chairman of the Board and Chief Executive Officer ( **CEO** ) and our Executive Vice President and Chief Financial Officer ( **CFO** ), as appropriate to allow timely decisions regarding required disclosure.

We have performed an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures under the supervision and with the participation of our management, including our CEO and CFO. Based

on that evaluation, our CEO and CFO have concluded that, as of the end of the period covered by this quarterly report, our disclosure controls and procedures were effective to provide reasonable assurance that material information relating to our Company and our consolidated subsidiaries was made known to them by others within those entities before or during the period in which this quarterly report was being prepared.

In designing and evaluating our disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, as ours are designed to do. Management also noted that the design of any system of controls is also based in part upon certain assumptions about the likelihood of future events, and that there can be no assurance that any such design will succeed in achieving its stated goals under all potential future conditions, regardless of how remote. Management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

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**Changes in Internal Controls**

We also maintain a system of internal control over financial reporting that is designed by, or under the supervision of, our CEO and CFO, and effected by management and other personnel, with the objective of providing reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States and includes those policies and procedures that:

pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of our assets;

provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and

provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

As directed by Section 404 of the Sarbanes-Oxley Act of 2002, the SEC adopted rules (Release No. 33-8238) requiring us to include in our Form 10-K for the fiscal year ending September 30, 2005, and each subsequent Form 10-K, a report of management on internal control over financial reporting and a related report of our independent auditors. Management's report must include its assessment of the effectiveness of our internal control over financial reporting as of the end of the applicable fiscal year. Our independent auditor must examine management's assessment of internal control over financial reporting and attest whether management's assessment of effectiveness is fairly stated in all material respects. The auditor's report must also evaluate whether our internal control structure provides reasonable assurance that transactions are recorded as necessary, among other requirements. So that they will be prepared to include these reports in our Annual Report on Form 10-K for the fiscal year ended September 30, 2005, management is engaged in an ongoing process of evaluating and improving our internal control over financial reporting. During the period covered by this quarterly report, we have made no change in our internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. Nevertheless, there can be no assurance that changes we might make to our internal control over financial reporting as part of this ongoing process will not, individually or in the aggregate, materially affect, or be reasonably likely to materially affect, our internal control over financial reporting.

**PART II. OTHER INFORMATION**

**Item 4. Submission of Matters to a Vote of Security Holders**

We held our annual meeting of shareholders on January 23, 2004 at which we submitted several matters to a vote of our shareholders:

**(a) Election of Directors**

Votes cast for or withheld regarding four individuals nominated for election to serve on our board of directors for a term expiring in 2007 were as follows:

**For**

**Withheld**

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|                        |            |           |
|------------------------|------------|-----------|
| Stephen G. Anderson    | 27,757,671 | 723,931   |
| Robert B. Currey       | 27,776,261 | 705,341   |
| L. L. Gellerstedt, III | 27,367,272 | 1,114,330 |
| John W. Spiegel        | 27,370,770 | 1,110,832 |

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Votes cast for or withheld regarding one individual nominated for election to serve on our board of directors for a term expiring in 2006 were as follows:

|                | <u>For</u> | <u>Withheld</u> |
|----------------|------------|-----------------|
| James E. Young | 27,848,082 | 633,520         |

Additional directors, whose term of office as directors continued after the meeting, are as follows:

| <u>Term expiring in 2005</u> | <u>Term expiring in 2006</u> |
|------------------------------|------------------------------|
| J. Hyatt Brown               | John D. Hopkins              |
| Russell M. Currey            | James W. Johnson             |
| G. Stephen Felker            | James A. Rubright            |

**(b) Other Matters**

Votes cast for or against, as well as the number of abstentions and broker non-votes regarding each other matter voted upon at the meeting, were as follows:

|  | <u>For</u> | <u>Against</u> | <u>Abstain</u> | <u>Broker<br/>Non-Vote</u> |
|--|------------|----------------|----------------|----------------------------|
| Approval of amendment to 1993 Employee Stock Purchase Plan | 23,158,633 | 1,096,798      | 1,225,854      | 3,000,317                  |

**Item 6. EXHIBITS AND REPORTS ON FORM 8-K****(a) Exhibits**

**See separate Exhibit Index attached hereto and hereby incorporated herein.**

**(b) Reports on Form 8-K**

During the second quarter of fiscal 2004, we filed the following Current Reports on Form 8-K: none.

During the second quarter of fiscal 2004, we furnished to the SEC the following Current Reports on Form 8-K:

1. Form 8-K furnished January 21, 2004.



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**SIGNATURES**

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

ROCK-TENN COMPANY  
(Registrant)

Date: May 13, 2004

By: /s/ Steven C. Voorhees  
Steven C. Voorhees  
Executive Vice President & Chief  
Financial Officer (Principal Financial  
Officer, Chief Accounting Officer and  
duly authorized officer)

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**ROCK-TENN COMPANY**

**INDEX TO EXHIBITS**

- Exhibit 3.1 Restated and Amended Articles of Incorporation of the Registrant (incorporated by reference to Exhibit 3.1 to the Registrant's Registration Statement on Form S-1, File No 33-73312)
- Exhibit 3.2 Articles of Amendment to the Registrant's Restated and Amended Articles of Incorporation (incorporated by reference to Exhibit 3.2 of the Registrant's Annual Report on Form 10-K for the year ended September 30, 2000)
- Exhibit 3.3 Bylaws of the Registrant (incorporated by reference to Exhibit 3.3 of the Registrant's Annual Report on Form 10-K for the year ended September 30, 2003)
- Exhibit 4.1 The rights of the Registrant's equity security holders are defined in Article II of the Restated and Amended Articles of Incorporation of the Registrant and Article II of the Articles of Amendment to the Registrant's Restated and Amended Articles of Incorporation. See Exhibits 3.1 and 3.2
- Exhibit 31.1 Certification Accompanying Periodic Report Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, executed by James A. Rubright, Chairman of the Board and Chief Executive Officer of Rock-Tenn Company.
- Exhibit 31.2 Certification Accompanying Periodic Report Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, executed by Steven C. Voorhees, Executive Vice President and Chief Financial Officer of Rock-Tenn Company.

**Additional Exhibits.**

In accordance with SEC Release No. 33-8238, Exhibit 32.1 is to be treated as accompanying this report rather than filed as part of the report.

- Exhibit 32.1 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, executed by James A. Rubright, Chairman of the Board and Chief Executive Officer of Rock-Tenn Company, and by Steven C. Voorhees, Executive Vice President and Chief Financial Officer of Rock-Tenn Company.

The Registrant agrees to furnish to the Securities and Exchange Commission, upon request, a copy of any instrument defining the rights of holders of long-term debt of the Registrant and all of its consolidated subsidiaries and unconsolidated subsidiaries for which financial statements are required to be filed with the Securities and Exchange Commission.