

[A. SCHULMAN LOGO]

**2002 ANNUAL REPORT**

**Traditional Values**  
**State-of-the-Art Solutions**

## About the Company

A. Schulman Inc. is a leading international supplier of high-performance plastic compounds and resins, which are used as a raw material by the Company's customers. The Company's principal product lines consist of proprietary and custom-formulated engineered plastic compounds, color concentrates and additives that improve the appearance and performance of plastics in a number of specialized applications.

End-use markets include agriculture; appliances; electronics and telecommunications; automotive/transportation; building/construction; general film, fiber and packaging; furniture and housewares; lawn and garden; medical/hygiene; sports and leisure; toys; and a variety of other industrial and consumer products.

A. Schulman has technology centers in North America and Europe devoted to new product development and color research. The Company's manufacturing facilities have their own product testing and quality control laboratories to ensure timely delivery of high-quality products to A. Schulman's global customer base.

Headquartered in Akron, Ohio, A. Schulman employs approximately 2,400 people and has 13 manufacturing facilities in North America, Europe and the Asia-Pacific region. A. Schulman stock is quoted through the NASDAQ National Market System (Symbol: SHLM).

## ABOUT THE THEME

A. Schulman offers a unique combination of Traditional Values and State-of-the-Art Solutions. Our strong commitment to profitable growth, fiscal responsibility and conservative management of the business provides us with the cash flow and resources necessary to invest in technology and rapidly develop and bring to market innovative, high-performance polymer products worldwide.

[PHOTO OF ROWS OF TOMATO PLANTS COVERED BY VARIOUS COLORS OF PLASTIC MULCH]

A growing part of A. Schulman's business is agricultural applications, which demonstrate the Company's capabilities in concentrates, color technology and environment-friendly products. In this photo: Various colors of plastic mulch are used to aid tomato growth and flavor, and improve nutrient content — all without negatively impacting the environment.

**Financial Highlights**

	Year Ended August 31,		
	2002	2001	2000
Net sales	\$966,593,000	\$975,221,000	\$1,032,519,000
Net income <sup>(1)(2)</sup>	\$ 32,154,000	\$ 12,692,000	\$ 37,704,000
Diluted earnings per share <sup>(1)(2)</sup>	\$ 1.08	\$ 0.43	\$ 1.25
Capital expenditures	\$ 26,765,000	\$ 33,374,000	\$ 32,452,000
Long-term debt and other non-current liabilities	\$124,509,000	\$144,657,000	\$ 123,086,000
Long-term liabilities to capital	25.9%	31.0%	27.6%
Stockholders' equity	\$356,361,000	\$322,079,000	\$ 323,461,000
Book value per common share	\$ 12.08	\$ 10.99	\$ 10.99
Number of stockholders of record	674	763	822
<b>Cash dividends per share</b>			
1st Quarter	\$ .135	\$ .135	\$ .125
2nd Quarter	.135	.135	.135
3rd Quarter	.135	.135	.135
4th Quarter	.135	.135	.135
	<u>\$ .540</u>	<u>\$ .540</u>	<u>\$ .530</u>

**Common stock price range**

	High - Low	High - Low	High - Low
1st Quarter	\$ 13.92 - 8.98	\$ 12.63 - 8.94	\$19.00 - 14.44
2nd Quarter	18.70 - 12.59	14.00 - 9.25	16.88 - 12.19
3rd Quarter	24.78 - 16.87	13.20 - 10.55	14.38 - 11.13
4th Quarter	\$22.12 - 16.63	\$14.43 - 11.45	\$13.13 - 10.63

- (1) Year ended August 31, 2001 includes a charge of \$4,635,000 or \$.16 per share related to the cost of Akron, Ohio plant closure.
- (2) Year ended August 31, 2000 includes income of \$2,535,000 or \$.07 per share from demutualization of an insurance company and the settlement of an insurance claim resulting from equipment problems at a North American facility.

## To Our Stockholders:

[PHOTO OF TERRY L. HAINES AND ROBERT A. STEFANKO]

TERRY L. HAINES AND ROBERT A. STEFANKO AT THE NORTH AMERICAN CUSTOMER SALES SUPPORT CENTER IN AKRON, OHIO.

We are pleased to report a significant improvement in earnings during the 2002 fiscal year. We saw the positive results of our actions over the last few years. We have rationalized product lines, consolidated manufacturing of certain products and maintained control of our expenditures. Our business systems are providing benefits and serving our customers on a timely and efficient basis throughout the world.

Traditional values are important to all of us. Over the years, A. Schulman, Inc. has established a reputation for its fiscal responsibility, conservative management style, profitability and strong financial position. Equally important is our approach to state-of-the-art solutions for customers throughout the world. We have continued to invest in technology and new product development.

We believe this focus on traditional values and state-of-the-art solutions will enable us to achieve continuing success in today's extremely competitive marketplace.

## OVERVIEW OF FINANCIAL RESULTS

Net income for the fiscal year ended August 31, 2002 was \$32,154,000 or \$1.08 per share on a diluted basis compared with earnings of \$12,692,000 or \$.43 per share for fiscal 2001. Last year's earnings included a charge of \$4,635,000 or \$.16 per share for the costs of closing our Akron, Ohio manufacturing facility.

Sales for the year were \$966.6 million compared with sales of \$975.2 million for fiscal 2001. Tonnage increased 3.2% for the year and the translation effect of foreign currencies increased sales by \$15.9 million or 1.6%. However, these increases were more than offset by lower prices and changes in product mix, which reduced sales by 5.7%.

Net income for the fiscal 2002 fourth quarter ended August 31, 2002 was \$10,783,000 or \$.36 per share on a diluted basis compared with earnings of \$5,511,000 or \$.19 per share for the same quarter last year.

It is gratifying that despite the difficulties in the current economic environment, there was a significant improvement in earnings for the final quarter of fiscal 2002, as well as the full year. The primary reasons for the significant increase in earnings were higher tonnage worldwide, an improvement in our gross profit margins and a favorable impact from the translation effect of foreign currencies, mainly the euro.

Sales for the fourth quarter were \$255.3 million, a 12.4% increase over sales of \$227.1 million for the same quarter last year. Tonnage was up 7.2% for the quarter, but lower pricing and changes in product mix reduced sales by 1%. The translation effect of currencies increased sales by \$14.1 million or 6.2% primarily due to the favorable impact from the euro, which appreciated significantly during the quarter.

The translation effect of foreign currencies increased net income by \$1.0 million or \$.04 per share for the fourth quarter and \$1.1 million or \$.04 per share for the 2002 fiscal year.

## EUROPE AND NORTH AMERICA

Profits were up in both Europe and North America for the fourth quarter.

European operating income for the quarter was up \$8.4 million, which represented approximately 82% of the worldwide increase of \$10.2 million. Tonnage in Europe was up 2.6% and gross profit margins improved to 20.6% compared with 16.8% in the fourth quarter of last year. The primary reasons for the improvement in margins were lower material costs and higher sales prices.

North American operating income increased \$1.5 million for the quarter and \$9.9 million for the fiscal year, a significant improvement compared with 2001 results. There was a strong increase in margins for both the fourth quarter and the full fiscal year. Gross profit margins for the quarter were 13.2% compared with 11.9% last year, and 14% for the 2002 fiscal year compared with 10.6% last year. Tonnage increased 14.6% for the quarter and 2.8% for the year.

## **EFFECTIVE TAX RATE**

The effective tax rate for fiscal 2002 was 44.2% compared with 56% last year. The rates are higher than the statutory rate of 35% because no tax benefits have been recognized on losses in the United States. The fiscal 2001 effective rate was higher than in 2002 due to the \$4,635,000 provision for closing the Akron plant in 2001 and a reduction in U.S. losses during fiscal 2002.

## **CAPITAL INVESTMENTS**

Capital expenditures for fiscal 2002 were \$26.8 million. During the year, we completed a \$15 million project at our German facility, which adds 33 million pounds of capacity as well as additional plant and warehousing space. At our Mexican facility, we are adding capacity for color concentrates that should be completed in early fiscal 2004. We have also renovated and modernized our Italian manufacturing facility, which we purchased in 2000. These improvements will enable us to expand our range of products and provide new efficiencies for this facility.

We recently announced our intention to build a manufacturing facility in China. This facility will cost approximately \$7.4 million and should be operational in about 24 months. The initial manufacturing line will have an annual capacity of approximately 40 million pounds and we will manufacture products for customers serving China's film, packaging and automotive markets. We are excited about the prospects for this new facility, which will provide a number of new opportunities for future growth.

## **FINANCIAL STRENGTH**

We further strengthened our already strong balance sheet during the past year. Total working capital was \$301 million, \$12 million higher than last year. Our current ratio is 3.5 and long-term debt of \$81 million is only 23% of total stockholders' equity. Stockholders' equity increased \$34 million to \$356 million for the year.

Our cash flow and the strength of our balance sheet provide us with the funds necessary to finance future expansions and the capability to meet new and challenging demands of the marketplace. In today's rapidly changing market, it's difficult to effectively compete internationally without a sound and growing financial base.

## **CASH DIVIDENDS**

Cash dividends paid on common stock were \$.54 per share for the years ended August 31, 2002 and 2001. In October 2002, the board declared the regular quarterly dividend of \$.135 per share. Our consistent record of dividend payments reflects our financial strength and our intention to continue to reward shareholders for the success of A. Schulman.

## **MANAGEMENT**

In October 2002, we further strengthened our European management team with the appointment of Jack Taylor as Associate General Manager of Europe. Mr. Taylor has been with A. Schulman since 1978 and has held a number of management positions, including General Manager of our United Kingdom operations. He has a broad range of experience, especially in sales and manufacturing. His know-how and experience will be an important asset to our already strong team in Europe.

## **PASSING OF BOARD MEMBER**

We were deeply saddened when Alan Ockene, a member of our board since 1992, passed away in August 2002. All of us will miss his experience, dedication and, most of all, his friendship.

## **BUSINESS OUTLOOK**

Our business continues to be quite good in our international operations, particularly Europe. Although there has been some moderation of growth in these economies, demand is good and we have a solid level of orders.

In the latter part of our fiscal 2002 fourth quarter, there was some softening of orders in North America. There had also been weaker than anticipated sales in September and early October, although we saw some strengthening as the month progressed.

While we are concerned by these current conditions in North America, our plan provides for improved results for the 2003 fiscal year. The new fiscal year will bring many new challenges, but we are confident that the actions we have taken have positioned us to achieve continuing gains in the years ahead.

We appreciate the dedication and efforts of our employees worldwide, and the confidence of our customers in our ability to meet their needs. We would also like to thank our stockholders and others for their continued interest in A. Schulman.

/s/ Terry L. Haines

Terry L. Haines  
President and Chief Executive Officer

/s/ Robert A. Stefanko

Robert A. Stefanko  
Chairman

November 1, 2002

# Traditional Values

## State-of-the-Art Solutions

A. Schulman's *commitment to traditional values* is evident in its cash flow and strong balance sheet, fiscal responsibility, focus on profitable growth, and realistic, conservative management of the business. The Company has consistently paid a dividend, and continues to invest in leading-edge technology, new product development, next-generation applications, and growth markets.

### OPPORTUNITIES IN GROWTH MARKETS

A. Schulman produces high-performance products for growth markets worldwide. To meet increasing European demand for film and packaging products, during fiscal 2002, the Company added capacity at its German facility. The Company also completed renovations at its manufacturing facility in Italy, one of the world's largest and fastest-growing plastics markets, and plans to build a manufacturing facility in Poland.

The Company will also build a manufacturing facility in China to capitalize on new business opportunities in the Chinese plastics market, which is growing approximately 20 percent annually.

A. Schulman is adding color concentrates capacity at its Mexican facility to support Mexico's increasingly sophisticated molders and extruders of plastic materials. The Company continues to refine its product mix and expand its film and packaging capabilities to North American markets. Its Product Technology Center and Color Technology Center in Akron, Ohio are centers of excellence for the development of new products and applications.

[PHOTO OF MOTHER AND DAUGHTER IN KITCHEN MAKING LUNCH]

A. Schulman's Polybatch family of products offers easier processability, faster speed and better economies of scale than traditional plastic film technology. An important application for PolyBatch is plastic bread bags used throughout the world markets. This packaging provides resistance to moisture and ensures freshness of product. In addition to food packaging, plastic films are often produced in breathable configurations for use in diapers, health care and personal hygiene products.

## **FILM LAMINATE APPLICATIONS**

A. Schulman holds a leadership position in molded-in film laminates, which meet strict performance criteria for strength, weatherability and color. The materials are used particularly in the automotive industry — for bumpers, side panels and other exterior components. The paint film chemically bonds to plastic parts during the injection molding process — a less costly, environment-friendly alternative to paint shops that also satisfies consumer demand for quality and durability.

## **INVISION — A PVC ALTERNATIVE**

Invision is a practical, high-technology, environmentally friendly alternative to polyvinyl chloride. Invision addresses market demand for PVC-free compounds that are lightweight and soft without sacrificing scratch resistance, weatherability, colorability, moisture resistance and other critical performance characteristics. Applications include handles, grips and trim for the automotive, furniture and other markets. Since introducing Invision in the automotive industry in 2001, A. Schulman has received more than a dozen platform approvals for automotive interiors.

## **CONCENTRATES THAT PERFORM**

A. Schulman's thermoplastic additive and color concentrates improve the appearance and performance of polymers. The Company develops materials to address customers' exact performance criteria, then ensures that the criteria, including custom colors and exact color matches, are used throughout its worldwide manufacturing operations. This enables A. Schulman to serve global customers' needs for consistency in material performance and look.

## **ENGINEERED PLASTICS**

A. Schulman develops specialty compounds and composite materials that are strong but lightweight, offer design flexibility, and are easy and inexpensive for the customer to use. For the appliance and tool industries, product attributes include electrical and/or thermal conductivity, and fire retardancy. In housewares, lawn and garden, and sports and leisure products, the focus is on durability and/or weatherability.

[PHOTO OF TWO CHILDREN IN PILE OF PUMPKINS IN THE FOREGROUND  
AND FATHER AT BACK OF SUV IN BACKGROUND]

The Cadillac Escalade EXT features A. Schulman's advanced molded-in film laminates and other polymer products. A. Schulman content on this luxurious, high-performance vehicle includes the claddings, running boards, tool box components, and structures surrounding the rear window and exterior mirrors.

A. Schulman, Inc.

**Consolidated Statement of Income**

	Year Ended August 31,		
	2002	2001	2000
<b>Net Sales</b>	\$966,593,000	\$975,221,000	\$1,032,519,000
<b>Interest and Other Income</b>	2,179,000	1,969,000	6,703,000
<b>Total</b>	<u>968,772,000</u>	<u>977,190,000</u>	<u>1,039,222,000</u>
<b>Costs and Expenses:</b>			
Cost of sales	806,260,000	846,592,000	865,357,000
Selling, general and administrative expenses	97,655,000	94,535,000	97,893,000
Interest expense	5,531,000	7,087,000	6,235,000
Foreign currency transaction (gains) losses	459,000	(1,043,000)	(500,000)
Minority interest	1,286,000	1,155,000	2,138,000
	<u>911,191,000</u>	<u>948,326,000</u>	<u>971,123,000</u>
<b>Income Before Taxes</b>	57,581,000	28,864,000	68,099,000
<b>Provision for U.S. and Foreign Income Taxes</b>	25,427,000	16,172,000	30,395,000
<b>Net Income</b>	<u>\$ 32,154,000</u>	<u>\$ 12,692,000</u>	<u>\$ 37,704,000</u>
<b>Weighted-average Number of Shares Outstanding:</b>			
Basic	29,296,435	29,184,605	30,224,433
Diluted	29,667,037	29,199,566	30,224,433
<b>Earnings per Share of Common Stock:</b>			
Basic	\$ 1.10	\$ 0.43	\$ 1.25
Diluted	\$ 1.08	\$ 0.43	\$ 1.25

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

A. Schulman, Inc.

**Consolidated Statement of Stockholders' Equity**

	Preferred Stock	Common Stock	Other Capital	Accumulated Other Comprehensive Income
Balance at August 31, 1999	\$1,069,000	\$38,381,000	\$46,694,000	\$(17,191,000)
Comprehensive income for 2000:				
Net income for 2000				
Foreign currency translation loss				(30,260,000)
Minimum pension liability adjustment (net of tax of \$297,000)				(552,000)
Total comprehensive income				
Cash dividends paid or accrued:				
Preferred stock, \$5 per share				
Common stock, \$.53 per share				
Purchase of treasury stock				
Redemption of preferred stock	(12,000)			
Grant of restricted stock			958,000	
Amortization of restricted stock				
Balance at August 31, 2000	1,057,000	38,381,000	47,652,000	(48,003,000)
Comprehensive income for 2001:				
Net income for 2001				
Foreign currency translation gain				2,683,000
Minimum pension liability adjustment (net of tax of \$220,000)				375,000
Total comprehensive income				
Cash dividends paid or accrued:				
Preferred stock, \$5 per share				
Common stock, \$.54 per share				
Purchase of treasury stock				
Issue of restricted stock		43,000	(280,000)	
Grant of restricted stock			1,132,000	
Amortization of restricted stock				
Balance at August 31, 2001	1,057,000	38,424,000	48,504,000	(44,945,000)
Comprehensive income for 2002:				
Net income for 2002				
Foreign currency translation gain				13,740,000
Minimum pension liability adjustment (net of tax of \$14,000)				(25,000)
Total comprehensive income				
Cash dividends paid or accrued:				
Preferred stock, \$5 per share				
Common stock, \$.54 per share				
Stock options exercised		206,000	3,370,000	
Grant of restricted stock			100,000	
Amortization of restricted stock				
Balance at August 31, 2002	\$1,057,000	\$38,630,000	\$51,974,000	\$(31,230,000)

[Additional columns below]

[Continued from above table, first column(s) repeated]

	Retained Earnings	Treasury Stock	Unearned Stock Grant Compensation	Total Stockholders' Equity
Balance at August 31, 1999	\$427,880,000	\$(138,291,000)	\$(2,296,000)	\$356,246,000
Comprehensive income for 2000:				
Net income for 2000	37,704,000			
Foreign currency translation loss				
Minimum pension liability adjustment (net of tax of \$297,000)				
Total comprehensive income				6,892,000
Cash dividends paid or accrued:				
Preferred stock, \$5 per share	(53,000)			(53,000)
Common stock, \$.53 per share	(16,163,000)			(16,163,000)
Purchase of treasury stock		(24,100,000)		(24,100,000)
Redemption of preferred stock				(12,000)
Grant of restricted stock			(958,000)	—
Amortization of restricted stock			651,000	651,000
Balance at August 31, 2000	449,368,000	(162,391,000)	(2,603,000)	323,461,000
Comprehensive income for 2001:				
Net income for 2001	12,692,000			
Foreign currency translation gain				
Minimum pension liability adjustment				

(net of tax of \$220,000)				
Total comprehensive income				15,750,000
Cash dividends paid or accrued:				
Preferred stock, \$5 per share	(53,000)			(53,000)
Common stock, \$.54 per share	(15,865,000)			(15,865,000)
Purchase of treasury stock		(1,840,000)		(1,840,000)
Issue of restricted stock				(237,000)
Grant of restricted stock			(1,132,000)	—
Amortization of restricted stock			863,000	863,000
Balance at August 31, 2001	446,142,000	(164,231,000)	(2,872,000)	322,079,000
Comprehensive income for 2002:				
Net income for 2002	32,154,000			
Foreign currency translation gain				
Minimum pension liability adjustment (net of tax of \$14,000)				
Total comprehensive income				45,869,000
Cash dividends paid or accrued:				
Preferred stock, \$5 per share	(53,000)			(53,000)
Common stock, \$.54 per share	(15,973,000)			(15,973,000)
Stock options exercised				3,576,000
Grant of restricted stock			(100,000)	—
Amortization of restricted stock			863,000	863,000
Balance at August 31, 2002	<u>\$462,270,000</u>	<u>\$(164,231,000)</u>	<u>\$(2,109,000)</u>	<u>\$356,361,000</u>

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

A. Schulman, Inc.  
**Consolidated Balance Sheet**

	August 31, 2002	August 31, 2001
<b>ASSETS</b>		
<b>Current Assets:</b>		
Cash and cash equivalents	\$ 63,984,000	\$ 52,586,000
Accounts receivable, less allowance for doubtful accounts of \$6,912,000 in 2002 and \$6,458,000 in 2001	172,327,000	162,131,000
Inventories, average cost or market, whichever is lower	169,719,000	159,808,000
Prepays, including tax effect of temporary differences	13,257,000	15,023,000
<b>Total Current Assets</b>	<b>419,287,000</b>	<b>389,548,000</b>
<b>Other Assets:</b>		
Cash surrender value of life insurance	352,000	639,000
Deferred charges, etc., including tax effect of temporary differences	8,474,000	11,247,000
Goodwill	6,558,000	6,520,000
Intangible assets	545,000	1,110,000
	15,929,000	19,516,000
<b>Property, Plant and Equipment, at cost:</b>		
Land and improvements	11,408,000	10,978,000
Buildings and leasehold improvements	103,536,000	83,039,000
Machinery and equipment	254,431,000	222,554,000
Furniture and fixtures	26,811,000	23,828,000
Construction in progress	6,625,000	26,415,000
	402,811,000	366,814,000
Accumulated depreciation and investment grants of \$937,000 in 2002 and \$884,000 in 2001	225,695,000	197,207,000
	177,116,000	169,607,000
	<b>\$612,332,000</b>	<b>\$578,671,000</b>

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

	August 31, 2002	August 31, 2001
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Current Liabilities:</b>		
Notes payable	\$ —	\$ 313,000
Current portion of long-term debt	413,000	267,000
Accounts payable	71,107,000	55,426,000
U.S. and foreign income taxes payable	6,751,000	7,097,000
Accrued payrolls, taxes and related benefits	22,688,000	19,036,000
Other accrued liabilities	17,373,000	18,121,000
<b>Total Current Liabilities</b>	<b>118,332,000</b>	<b>100,260,000</b>
<b>Long-term Debt</b>	<b>81,038,000</b>	<b>105,415,000</b>
<b>Other Long-term Liabilities</b>	<b>43,471,000</b>	<b>39,242,000</b>
<b>Deferred Income Taxes</b>	<b>6,957,000</b>	<b>6,115,000</b>
<b>Minority Interest</b>	<b>6,173,000</b>	<b>5,560,000</b>
<b>Stockholders' Equity:</b>		
Preferred stock, 5% cumulative, \$100 par value, authorized, issued and outstanding - 10,567 shares in 2002 and 2001	1,057,000	1,057,000
Special stock, 1,000,000 shares authorized, none outstanding	—	—
Common stock, \$1 par value		
Authorized - 75,000,000 shares		
Issued - 38,629,967 shares in 2002 and 38,423,967 shares in 2001	38,630,000	38,424,000
Other capital	51,974,000	48,504,000
Accumulated other comprehensive income	(31,230,000)	(44,945,000)
Retained earnings	462,270,000	446,142,000
Treasury stock, at cost, 9,211,095 shares in 2002 and 2001	(164,231,000)	(164,231,000)
Unearned stock grant compensation	(2,109,000)	(2,872,000)
<b>Common Stockholders' Equity</b>	<b>355,304,000</b>	<b>321,022,000</b>
<b>Total Stockholders' Equity</b>	<b>356,361,000</b>	<b>322,079,000</b>
	<b>\$ 612,332,000</b>	<b>\$ 578,671,000</b>

**Consolidated Statement of Cash Flows**

	Year Ended August 31,		
	2002	2001	2000
Provided from (used in) operating activities:			
Net income	\$ 32,154,000	\$ 12,692,000	\$ 37,704,000
Items not requiring the current use of cash:			
Depreciation	22,812,000	21,054,000	21,585,000
Non-current deferred taxes	1,954,000	(463,000)	(3,179,000)
Foreign pension and other deferred compensation	2,908,000	1,884,000	2,506,000
Postretirement benefit obligation	567,000	(1,347,000)	1,657,000
Write-off of assets — Akron, Ohio plant closure	—	3,230,000	—
Changes in working capital:			
Accounts receivable	3,414,000	4,350,000	(30,226,000)
Inventories	(4,570,000)	26,059,000	(28,083,000)
Prepays	2,306,000	1,374,000	2,685,000
Accounts payable	6,234,000	(9,803,000)	17,322,000
Income taxes	(869,000)	(2,635,000)	3,452,000
Accrued payrolls and other accrued liabilities	1,199,000	3,271,000	811,000
Changes in other assets and other long-term liabilities	2,380,000	(1,647,000)	(264,000)
Net cash provided from operating activities	<u>70,489,000</u>	<u>58,019,000</u>	<u>25,970,000</u>
Provided from (used in) investing activities:			
Expenditures for property, plant and equipment	(26,765,000)	(33,374,000)	(32,452,000)
Disposals of property, plant and equipment	605,000	998,000	1,941,000
Net cash used in investing activities	<u>(26,160,000)</u>	<u>(32,376,000)</u>	<u>(30,511,000)</u>
Provided from (used in) financing activities:			
Cash dividends paid	(16,026,000)	(15,918,000)	(16,216,000)
Decrease of notes payable	(323,000)	(7,663,000)	(1,989,000)
Reduction of long-term debt	(24,338,000)	(260,000)	—
Increase of long-term debt	—	22,000,000	19,075,000
Exercise of stock options	3,576,000	—	—
Investment grants from foreign countries	47,000	—	875,000
Increase in minority interest, net of distributions	613,000	630,000	1,538,000
Purchase of treasury stock	—	(1,840,000)	(24,100,000)
Redemption of preferred stock	—	—	(12,000)
Net cash used in financing activities	<u>(36,451,000)</u>	<u>(3,051,000)</u>	<u>(20,829,000)</u>
Effect of exchange rate changes on cash	3,520,000	3,128,000	(4,600,000)
Net increase (decrease) in cash and cash equivalents	11,398,000	25,720,000	(29,970,000)
Cash and cash equivalents at beginning of year	52,586,000	26,866,000	56,836,000
Cash and cash equivalents at end of year	<u>\$ 63,984,000</u>	<u>\$ 52,586,000</u>	<u>\$ 26,866,000</u>
Cash paid during the year for:			
Interest	\$ 5,362,000	\$ 6,908,000	\$ 6,063,000
Income Taxes	\$ 20,030,000	\$ 17,929,000	\$ 26,583,000

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

## Notes to Consolidated Financial Statements

### Note 1 — Summary of Significant Accounting Policies

#### Principles of Consolidation

The consolidated financial statements include the accounts of A. Schulman, Inc. and its domestic and foreign subsidiaries. All significant intercompany transactions have been eliminated.

Minority interest represents a 30% equity position of Mitsubishi Chemical MKV Co. in a partnership with the Company and a 35% equity position of P.T. Prima Polycon Indah in an Indonesian joint venture with the Company.

#### Cash Equivalents and Short-Term Investments

All highly liquid investments purchased with a maturity of three months or less are considered to be cash equivalents. Such investments amounted to \$35,824,000 at August 31, 2002 and \$20,991,000 at August 31, 2001. Investments with maturities between three and 12 months are considered to be short-term investments. Investments are placed with numerous financial institutions having good credit ratings. The recorded amount of these investments approximates fair value.

#### Revenue Recognition

The Company's accounting policy regarding revenue recognition is to recognize revenue when products are shipped to unaffiliated customers. The Company provides tolling services as a fee for processing of material provided and owned by customers. On some occasions, the Company is required to provide certain amounts of its materials, such as additives or packaging. These materials are charged to the customer as an addition to the tolling fees. The only amounts recorded as revenue related to tolling are the processing fees and the charges related to materials provided by the Company.

#### Depreciation

It is the Company's policy to depreciate the cost of property, plant and equipment over the estimated useful lives of the assets generally using the straight-line method. The estimated useful lives used in the computation of depreciation are as follows:

Buildings and leasehold improvements	10 to 40 years
Machinery and equipment	5 to 10 years
Computer equipment	3 to 5 years
Furniture and fixtures	10 years

The cost of property sold or otherwise disposed of is eliminated from the property accounts and the related reserve accounts, with recognition of gain or loss.

Maintenance and repair costs are charged against income. The cost of renewals and betterments is capitalized in the property accounts.

#### Inventories

The Company and its subsidiaries do not distinguish between raw materials and finished goods because numerous products that can be sold as finished goods are also used as raw materials in the production of other inventory items.

#### Goodwill

On September 1, 2001 the Company adopted the provisions of SFAS No. 142, "Goodwill and Other Intangible Assets," and therefore ceased amortizing goodwill as of that date. Prior to the adoption of SFAS No. 142, the Company amortized goodwill, on a straight-line basis, over periods ranging from five years to 25 years. The Company conducts a formal impairment test of goodwill at the reporting unit level on an annual basis and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying value.

#### Income Taxes

Income taxes are recognized during the year in which transactions enter into the determination of financial statement income. Accordingly, deferred taxes are provided for temporary differences between the book and tax bases of assets and liabilities.

#### Retirement Plans

The Company has several defined benefit pension plans covering hourly employees in the U.S. and certain employees in foreign countries. For certain plans in the U.S., pension funding is based on an amount paid to trust funds at an agreed rate for each hour for which employees are paid. For one U.S. plan, the policy is to fund amounts to cover current cost and amortize prior service costs over approximately 30 years.

Generally, the foreign plans accrue the current and prior service costs annually. In certain countries, funding is not required and the liability for such pensions is included in other long-term liabilities.

The Company also has deferred profit sharing plans for its North American salaried employees for which contributions are determined at the discretion of the Board of Directors.

**Foreign Currency Translation**

The financial position and results of operations of the Company's foreign subsidiaries, except those subsidiaries located in highly inflationary economies, are measured using local currency as the functional currency. Assets and liabilities of these subsidiaries are translated at the exchange rate in effect at each year-end. Income statement accounts are translated at the average rate of exchange prevailing during the year. Accumulated other comprehensive income in stockholders' equity includes translation adjustments arising from the use of different exchange rates from period to period.

**Use of Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles 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.

**Reclassification**

Certain items previously reported in specific financial statement captions have been reclassified to conform to the 2002 presentation.

**Stock-Based Compensation**

As provided for under Statement of Financial Accounting Standards No. 123, "Accounting for Stock Based Compensation" (SFAS 123), the Company has elected to continue to account for stock-based compensation under the provisions of Accounting Principles Boards Opinion No. 25, "Accounting for Stock Issued to Employees." Compensation cost for stock options is measured as the excess, if any, of the quoted market price of the Company's stock at the date of the grant over the amount an employee must pay to acquire the stock. Refer to Note 8.

**Notes to Consolidated Financial Statements****Derivative Instruments and Hedging Activities**

Effective September 1, 2000 the Company adopted Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" (SFAS 133) as amended and interpreted. The standard requires all derivatives, whether designated in hedging relationships or not, to be recorded on the balance sheet at fair value. Due to the short-term nature of the Company's forward exchange contracts, the derivatives were adjusted to their fair market value through the income statement. Gains or losses on forward contracts that hedge specific transactions are recognized in the consolidated statement of income offsetting the underlying foreign currency gains or losses. Due to the immaterial amount of derivative and hedging activity and the short-term nature of the derivatives outstanding, the effect of adopting SFAS 133 on the Company's results of operations and financial position was immaterial. Refer to Note 5.

**Note 2 — Goodwill and Other Intangible Assets**

On September 1, 2001, the Company adopted the provisions of SFAS No. 141 "Business Combinations," (SFAS No. 141) and SFAS No. 142, "Goodwill and Other Intangible Assets," (SFAS No. 142). SFAS No. 141 requires that all business combinations be accounted for by the purchase method and that certain acquired intangible assets be recognized as assets apart from goodwill. SFAS No. 142 provides that goodwill should not be amortized but instead be tested for impairment annually at the reporting unit level. In accordance with SFAS No. 142, the Company completed a transitional goodwill impairment test during the second quarter of fiscal 2002, which resulted in no impairment loss being recognized upon adoption. The Company also conducts a formal impairment test of goodwill at the reporting unit level on an annual basis and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying value. The annual test resulted in no impairment loss being recognized. Goodwill and intangible assets were reclassified from deferred charges for all reportable periods.

Accumulated amortization for intangibles was \$520,000, \$398,000 and \$131,000 at August 31, 2002, 2001 and 2000, respectively. Amortization expense for intangibles was \$308,000 in 2002, \$260,000 in 2001 and \$41,000 in 2000. There was no amortization expense for goodwill in 2002. Amortization expense for goodwill was \$578,000 or \$.02 per share in 2001 and \$572,000 or \$.02 per share in 2000. The Company does not anticipate any significant changes in amortization expense for intangibles in future periods.

The carrying amount of goodwill for the European segment was \$3,774,000 at August 31, 2002 and \$3,736,000 at August 31, 2001. The carrying amount of goodwill for the North American segment was \$2,784,000 at August 31, 2002 and 2001.

**Note 3 — Investment Grants**

The Company has received investment grants from various European countries. These grants have been provided to subsidize a portion of the Company's European manufacturing facilities. The total cost of the facilities has been included in plant and equipment and the amount of the grants has been included with accumulated depreciation in the financial statements. The entire cost of the facilities is depreciated over their estimated useful life and the investment grants are amortized against the related depreciation charges. The amortization of these grants amounted to \$62,000 in 2002, \$60,000 in 2001 and \$79,000 in 2000.

**Note 4 — Long-Term Debt and Credit Arrangements**

	August 31,	
	2002	2001
A. Schulman, Inc.:		
Revolving credit loan, 2.4% in 2002 and 3.91% in 2001	\$30,000,000	\$ 54,000,000
Senior notes, 7.27% due 2009	50,000,000	50,000,000
Capital lease obligations and other	1,038,000	1,415,000
	\$81,038,000	\$105,415,000

On October 2, 2001, the Company established a new four-year \$130,000,000 revolving credit agreement, replacing a \$100,000,000 facility in place at August 31, 2001. Under terms of the new agreement, the Company is required to satisfy certain financial and operating covenants including leverage ratio, interest coverage ratio and capitalization ratio. The revolving credit agreement is unsecured.

The Company has an outstanding Private Placement Agreement for \$50,000,000 of Senior Notes due in 2009. The interest rate is fixed at 7.27% and is payable quarterly with principal due upon maturity in 2009. In 1999, the Company completed an interest rate lock in order to reduce the interest cost over the life of the notes. Proceeds from this transaction totaling \$630,000 have been deferred and will be amortized over the life of the loan, effectively reducing the annual interest rate from 7.27% to 7.14%. Under this agreement, as of August 31, 2002, approximately \$44,000,000 of retained earnings was available for the payment of cash dividends. The Company's latest review of the covenants under these agreements indicate no defaults or any non-compliance with their covenants.

The Company has \$22,000,000 of unsecured short-term lines of credit from various domestic banks. There were no short-term borrowings under these facilities at August 31, 2002 and 2001.

The Company had \$33,390,000 of unsecured short-term foreign lines of credit available to its subsidiaries at August 31, 2002 and had \$42,840,000 available at August 31, 2001. There were no borrowings under these lines of credit at August 31, 2002 and \$313,000 at August 31, 2001 at a weighted- average interest rate of 15.00%.

The Company leases certain land and buildings for its European segment under a capital lease. The total amount due on this capital lease at August 31, 2002 is \$1,151,000.

Aggregate maturities of debt (including capital lease obligations) subsequent to August 31, 2002 are as follows:

Fiscal 2003	\$ 413,000
2004	413,000
2005	30,337,000
2006	288,000
2009	50,000,000
Total	<u>\$81,451,000</u>

## Note 5 — Foreign Currency Forward Contracts

The Company enters into forward foreign exchange contracts to reduce its exposure for amounts due or payable in foreign currencies. These contracts limit the Company's exposure to fluctuations in foreign currency exchange rates. Any gains or losses associated with these contracts as well as the offsetting gains or losses from the underlying assets or liabilities are recognized on the foreign currency transaction line in the Consolidated Statement of Income. The Company does not hold or issue foreign exchange contracts for trading purposes.

The following table presents a summary of foreign exchange contracts outstanding as of August 31, 2002 and August 31, 2001:

	2002		2001	
	Contract Amount	Fair Value	Contract Amount	Fair Value
Buy Currency:				
Euro	\$ 1,298,000	\$ 1,289,000	\$ 2,746,000	\$ 2,728,000
British pound	1,778,000	1,781,000	—	—
	<u>\$ 3,076,000</u>	<u>\$ 3,070,000</u>	<u>\$ 2,746,000</u>	<u>\$ 2,728,000</u>
Sell Currency:				
Euro	\$ —	\$ —	\$12,518,000	\$12,764,000
British pound	8,107,000	8,161,000	120,000	119,000
U.S. dollar	2,978,000	2,837,000	—	—
All other	1,862,000	1,851,000	—	—
	<u>\$12,947,000</u>	<u>\$12,849,000</u>	<u>\$12,638,000</u>	<u>\$12,883,000</u>

The fair value of foreign exchange contracts was estimated by obtaining quotes from banks. Foreign exchange contracts are entered into with several financial institutions having good credit ratings and generally have maturities of less than nine months.

## Note 6 — Income Taxes

Income (loss) before taxes is as follows:

	Year Ended August 31,		
	2002	2001	2000
Domestic	\$(13,127,000)	\$(20,780,000)	\$(4,231,000)
Foreign	70,708,000	49,644,000	72,330,000
	<u>\$ 57,581,000</u>	<u>\$ 28,864,000</u>	<u>\$68,099,000</u>

The provisions for U.S. and foreign income taxes consist of the following:

	Year Ended August 31,		
	2002	2001	2000
Current taxes:			
U.S	\$(1,164,000)	\$ 591,000	\$ 856,000
Foreign	21,292,000	15,134,000	27,862,000
	<u>20,128,000</u>	<u>15,725,000</u>	<u>28,718,000</u>
Deferred taxes:			
U.S	4,248,000	(130,000)	564,000
Foreign	1,051,000	577,000	1,113,000
	<u>5,299,000</u>	<u>447,000</u>	<u>1,677,000</u>
	<u>\$25,427,000</u>	<u>\$16,172,000</u>	<u>\$30,395,000</u>

A reconciliation of the statutory U.S. federal income tax rate with the effective tax rates of 44.2% in 2002, 56.0% in 2001 and 44.6% in 2000 is as follows:

(in thousands)	2002		2001		2000	
	Amount	% of Pretax Income	Amount	% of Pretax Income	Amount	% of Pretax Income
Statutory U.S tax rate	\$20,153	35.0%	\$10,102	35.0%	\$23,835	35.0%
Amount of foreign income taxes in excess of (less than) U.S. taxes at statutory rate	(2,471)	(4.3)	(3,705)	(12.8)	5,655	8.3
Loss with no benefit	9,592	16.7	9,245	32.0	1,481	2.2
Settlement of prior year liability	(2,013)	(3.5)	—	—	—	—
Other, net	166	.3	530	1.8	(576)	(.9)
	<u>\$25,427</u>	<u>44.2%</u>	<u>\$16,172</u>	<u>56.0%</u>	<u>\$30,395</u>	<u>44.6%</u>

Deferred tax assets and (liabilities) consist of the following at August 31, 2002 and August 31, 2001:

(in thousands)	2002	2001
Pensions	\$ 2,346	\$ 2,369
Inventory reserves	1,168	1,744
Bad debt reserves	1,225	1,378
Accruals	3,795	3,943
Postretirement benefits other than pensions	5,272	5,073
Foreign tax credit carryforwards	12,956	13,472
Alternative minimum tax carryforwards	4,513	2,590
Net operating loss carryforwards	—	3,782
Other	3,312	2,591
Gross deferred tax assets	<u>34,587</u>	<u>36,942</u>
Valuation allowance	<u>(23,423)</u>	<u>(19,828)</u>
Total deferred tax assets	<u>11,164</u>	<u>17,114</u>
Depreciation	<u>(13,478)</u>	<u>(13,552)</u>
Other	<u>(1,612)</u>	<u>(1,261)</u>
Gross deferred tax liabilities	<u>(15,090)</u>	<u>(14,813)</u>
	<u>\$ (3,926)</u>	<u>\$ 2,301</u>

The valuation allowance covers benefits for foreign tax credit carryforwards and other deferred tax assets in the United States which are not likely to be utilized. The foreign tax credit carryforwards will expire in periods from 2003 to 2007.

The tax effect of temporary differences included in prepaids was \$2,818,000 and \$6,638,000 at August 31, 2002 and 2001 respectively. Deferred charges included \$737,000 and \$2,182,000 from the tax effect of temporary differences at August 31, 2002 and 2001 respectively. The tax effect of temporary differences included in accrued liabilities was \$524,000 and \$405,000 at August 31, 2002 and 2001 respectively.

At August 31, 2002, no taxes have been provided on the undistributed earnings of certain foreign subsidiaries amounting to \$264,871,000 because the Company intends to reinvest these earnings.

## Notes to Consolidated Financial Statements

## Note 7 — Pension and Other Postretirement Benefit Plans

The Company has defined benefit pension plans and other postretirement benefit plans, primarily health care and life insurance. Benefits for the defined benefit plans are based primarily on years of service and qualifying compensation during the final years of employment. Postretirement health care and life insurance benefits are provided to certain domestic employees if they reach retirement age while working for the Company.

Components of the plan obligations and assets, and the recorded liability at August 31, 2002 and 2001 are as follows:

	Pension Benefits		Other Postretirement Benefits	
	2002	2001	2002	2001
Benefit obligation at beginning of year	\$(28,735,000)	\$(29,247,000)	\$(11,620,000)	\$(10,730,000)
Service cost	(1,111,000)	(1,064,000)	(696,000)	(590,000)
Interest cost	(1,837,000)	(1,786,000)	(825,000)	(738,000)
Participant contributions	(172,000)	(176,000)	—	—
Curtailement gain (loss)	—	(452,000)	—	1,235,000
Actuarial gain (loss)	(1,544,000)	1,389,000	(3,093,000)	(1,257,000)
Benefits paid	899,000	3,066,000	978,000	460,000
Translation adjustment	(2,291,000)	(465,000)	—	—
Benefit obligation at end of year	\$(34,791,000)	\$(28,735,000)	\$(15,256,000)	\$(11,620,000)
Fair value of plan assets at beginning of year	\$ 7,427,000	\$ 9,012,000	\$ —	\$ —
Actual return on assets	(607,000)	(687,000)	—	—
Employer contributions	1,240,000	2,015,000	978,000	460,000
Participant contributions	172,000	176,000	—	—
Benefits paid	(899,000)	(3,066,000)	(978,000)	(460,000)
Translation adjustment	421,000	(23,000)	—	—
Fair value of plan assets at end of year	\$ 7,754,000	\$ 7,427,000	\$ —	\$ —
Underfunded	\$(27,037,000)	\$(21,308,000)	\$(15,256,000)	\$(11,620,000)
Unamortized				
Net liability	427,000	568,000	—	—
Net (gain) loss	2,388,000	(545,000)	90,000	(3,099,000)
Prior year service cost	24,000	28,000	231,000	223,000
Net amount recognized	\$(24,198,000)	\$(21,257,000)	\$(14,935,000)	\$(14,496,000)
Amounts recognized in the statement of financial position consist of:				
Prepaid benefit cost	\$ 25,000	\$ 41,000	\$ —	\$ —
Accrued benefit liability	—	(295,000)	—	—
Intangible asset	—	(14,000)	—	—
Other long-term liabilities	(24,515,000)	(21,243,000)	(14,935,000)	(14,496,000)
Deferred income taxes	90,000	77,000	—	—
Accumulated other comprehensive income	202,000	177,000	—	—
	\$(24,198,000)	\$(21,257,000)	\$(14,935,000)	\$(14,496,000)

The components of net periodic benefit cost of the years ended August 31 are as follows:

Service cost	\$ 1,111,000	\$ 1,064,000	\$ 696,000	\$ 590,000
Interest cost	1,837,000	1,786,000	825,000	738,000
Expected return on plan assets	(633,000)	(786,000)	—	—
Amortization of transition obligation	141,000	175,000	—	—
Amortization of prior service cost	4,000	52,000	(8,000)	(32,000)
Deferred asset gain	—	—	(95,000)	(172,000)
Recognized net actuarial loss	—	87,000	—	—
Curtailement (gain) loss	—	1,600,000	—	(2,011,000)
	\$ 2,460,000	\$ 3,978,000	\$ 1,418,000	\$ (887,000)

The projected benefit obligation, accumulated benefit obligation, and fair value of plan assets for the pension plan with accumulated benefit obligations in excess of plan assets were \$34,791,000, \$30,182,000 and \$7,754,000 respectively as of August 31, 2002, and \$28,735,000, \$26,374,000 and \$7,427,000 respectively as of August 31, 2001. The underfunded position is primarily related to the Company's German pension plan, where funding is not required. The total pension contributions for multiemployer pension plans was \$140,000 in 2002, \$153,000 in 2001 and \$196,000 in 2000. The total cost for defined contribution plans was \$3,803,000 in 2002, \$3,436,000 in 2001 and \$3,603,000 in 2000.

Actuarial assumptions used in the calculation of the recorded liability are as follows:

	2002	2001
Weighted-average assumptions as of August 31		
Discount rate on pension plans	6.4%	6.4%
Discount rate on postretirement obligation	7.0%	7.3%
Return on pension plan assets	8.1%	8.2%
Rate of compensation increase	2.6%	2.5%
Projected health care cost trend rate	10.0%	10.0%
Ultimate health care rate	5.0%	5.0%
Year ultimate health care trend rate is achieved	2007	2007

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plan. A one-percentage point change in assumed health care cost trend rates would have the following effects at August 31, 2002:

	One-Percentage-Point Increase	One-Percentage-Point Decrease
Effect on total of service and interest cost components	\$ 266,000	\$ (219,000)
Effect on postretirement obligation	\$1,799,000	\$(1,586,000)

The Company has agreements with two current employees that upon retirement, or death or disability prior to retirement, it shall make 10 payments of \$100,000 each to two employees or their beneficiaries for a 10-year period and is 100% vested. The liability required for these agreements was fully accrued as of August 31, 2001. The Company provided \$66,000 and \$180,000 in 2001 and 2000, respectively, to cover the current cost for such agreements. In connection with such agreements, the Company owns and is the beneficiary of life insurance policies amounting to \$2,000,000. The amounts provided are included in other long-term liabilities.

#### Note 8 — Incentive Stock Plans

Effective in December 1991, the Company adopted the 1991 Stock Incentive Plan and authorized 1,875,000 shares for future grants. In October 1999, the plan was amended to authorize an additional 2,000,000 shares. The 1991 Plan provides for the grant of incentive stock options, nonqualified stock options and restricted stock awards. The option price of incentive stock options is the fair market value of the common shares on the date of grant. In the case of nonqualified stock options, the Company intends to grant options at fair market value on the date of grant. However, the Plan does provide that the option price may not be less than 50% of the fair market value of the common shares on the date of grant. Stock options may be exercised as determined by the Company, but in no event prior to six months following the date of grant or after the 10th anniversary date of grant.

Effective in October 1992, the Company adopted the 1992 Non-Employee Directors' Stock Option Plan and authorized 125,000 shares for future grants. In December 2000, the plan was amended to provide for the grant of 2,000 nonqualified stock options and 500 restricted stock awards to each non-employee director on the first business day of February of each year. The option price is the fair market value of the common shares on the first business day immediately preceding the date of grant. All options become exercisable at the rate of 25% per year, commencing on the first anniversary of the date of grant of the option. Each option expires five years from the date of grant.

Both the 1991 and 1992 Plans have expired and no further shares are available for issuance.

The following is a summary with respect to nonqualified stock option activity for all of the plans:

	Year Ended August 31,			
	2002		2001	
	Weighted Shares Under Option	Average Exercise Price	Weighted Shares Under Option	Average Exercise Price
Outstanding at beginning of year	2,031,300	\$15.20	1,646,569	\$16.85
Granted during the year	16,000	16.69	616,000	13.13
Exercised during the year	(206,000)	17.36	—	—
Cancelled during the year	(131,875)	17.88	(231,269)	21.16
Outstanding at end of year	1,709,425	14.75	2,031,300	15.20
Exercisable at end of year	900,506	15.93	749,469	17.46

The following table summarizes information about nonqualified stock options outstanding at August 31, 2002:

Grant Date	Options Outstanding	Options Exercisable	Weighted Average	
			Exercise Price	Remaining Life (Years)
7/98	239,200	239,200	18.91	0.8
7/99	333,275	249,956	18.31	1.8
8/00	488,450	244,225	12.13	3.0
8/01	598,500	149,625	13.17	4.0
All other	50,000	17,500	15.83	2.4

Under the 1991 Plan, restricted stock awards were as follows: 67,100 shares were granted on July 8, 1998, 52,800 were granted on July 8, 1999, 79,000 were granted on August 30, 2000, 85,000 were granted on August 31, 2001 and 3,000 were granted on October 19, 2001. The fair market value on the date of grant in fiscal year 1998 was \$18.91 per share, 1999 was \$18.31 per share, 2000 was \$12.13

per share, 2001 was \$13.17 per share and 2002 was \$10.97 per share. These shares vest five years following the date of grant so long as the holder remains employed by the Company. Unearned compensation representing the fair market value of the shares at the date of grant is charged to income over the five-year vesting period. Compensation expense for restricted stock was \$863,000 in 2002, \$626,000 in 2001 and \$650,000 in 2000.

No expense has been charged to income relating to stock options. If the fair value method of accounting for stock options under SFAS 123 had been used, the after-tax expense relating to the stock options would have been \$910,000, or \$.03 per share, in 2002, \$676,000, or \$.02 per share, in 2001 and \$761,000, or \$.03 per share, in 2000. Pro forma net income would have been \$31,244,000 in 2002, \$12,016,000 in 2001 and \$36,943,000 in 2000. The pro forma amounts listed above do not take into consideration the pro forma compensation expense related to grants made prior to fiscal 1997. The weighted-average fair value at the date of grant was \$3.96, \$3.23 and \$4.01 for options granted in 2002, 2001 and 2000, respectively.

**Notes to Consolidated Financial Statements**

Under SFAS 123, the fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model. The following weighted-average assumptions were used for grants:

	Year Ended August 31,		
	2002	2001	2000
Expected life (years)	5	5	5
Interest rate	4.3%	4.5 - 4.8%	5.9 - 6.7%
Volatility	43%	29%	30%
Dividend yield	3.2%	2.9%	1.32%

In October 2002, the Board of Directors authorized 4 million shares for nonqualified options and 500,000 shares for restricted stock under the new 2002 Equity Incentive Plan. Under this Plan, approximately 650,000 nonqualified options and 85,000 shares of restricted stock were granted on October 18, 2002 and are subject to stockholder approval. The exercise price of the options is \$13.99 per share, the fair market value on the date of the grant. This Plan will be submitted to stockholders for approval in December 2002.

**Note 9 — Earnings per Common Share**

Basic earnings per share is computed by dividing income available to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted earnings per share reflects the potential dilution that could occur if common stock equivalents were exercised and then shared in the earnings of the Company.

Under both the basic and diluted earnings per share calculations, reported net income is reduced by preferred dividends of \$53,000. The weighted-average number of common shares used is as follows:

	Year Ended August 31,		
	2002	2001	2000
Basic	29,296,435	29,184,605	30,224,433
Diluted	29,667,037	29,199,566	30,224,433

The difference between basic and diluted weighted-average common shares results from the assumed exercise of outstanding stock options and grants of restricted stock, calculated using the treasury stock method.

The following stock equivalents are not included in the diluted earnings per share calculation because their effects are antidilutive:

	Year Ended August 31,		
	2002	2001	2000
Stock equivalents	1,609,673	2,316,961	1,646,569

**Note 10 — Capital Stock and Stockholder Rights Plan**

The Special Stock of 1,000,000 shares was authorized with such preferences or special terms and for such consideration as may be determined at the discretion of the Board of Directors.

In January 1996, the Company adopted a Shareholder Rights Plan, and reserved 100,000 shares of Special Stock for use under such Plan. Under this Plan, one Right shall be attached to each share of Common Stock of the Company. Initially, the Rights are not exercisable and automatically trade with the Common Stock. However, 10 days after a person or group acquires 15% or more of the Company's Common Stock, or 10 business days after a person or group commences a tender or exchange offer that would result in such person or group owning 15% or more of the outstanding shares of Common Stock of the Company (even if no purchases actually occur), whichever is earlier, the Rights will become exercisable.

When the Rights first become exercisable, each Right will entitle the holder thereof to buy from the Company one share of Special Stock for \$85.00 (subject to adjustment thereafter). However, if any person or entity acquires 15% or more of the Company's Common Stock, each Right not owned by a 15%-or-more stockholder would become exercisable for a certain number of shares of Common Stock of the Company in lieu of one share of Special Stock. The number of shares of Common Stock would be that having at that time, a market value of two times the then current exercise price of the Right. If the Company is involved in a merger or other business combination with or into another person or entity in which the Company's Common Stock is changed into or exchanged for common stock of such other person or entity, or if the Company sells 50% or more of its assets or earning power to another person or entity, at any time after the Rights become exercisable, each Right will entitle the holder thereof to buy such number of shares of common stock of such other person or entity as have a market value of twice the then current exercise price of each Right.

The Company may redeem the Rights at a price of \$.01 per Right at any time prior to the 10th business day after public announcement of the acquisition by any person or entity of 15% or more of the Company's Common Stock. The Rights will expire on January 25, 2006 unless earlier redeemed by the Company. At no time will the Rights have any voting power.

**Note 11 — Leases**

Total rental expense was \$4,610,000 in 2002, \$4,456,000 in 2001 and \$4,217,000 in 2000. The future minimum rental commitments for non-cancelable leases excluding obligations for taxes, insurance, etc. are as follows:

Year ended August 31,	Minimum rental
2003	\$2,449,000
2004	2,080,000
2005	1,249,000
2006	510,000
2007	183,000
Later years	12,000
	\$6,483,000

**Note 12 — Segment Information**

The Company is engaged in the sale of plastic resins in various forms, which are used as raw materials by its customers. To identify reportable segments, the Company considered its operating structure and the types of information subject to regular review by executive management. On this basis, the Company operates primarily in two geographic business segments, North America and Europe.

The North American segment includes operations in the United States, Canada, and Mexico. The Company's European segment includes operations conducted in Belgium, France, Germany, Poland, Hungary, Indonesia, Italy, Spain, Switzerland and the United Kingdom. The accounting policies of each business segment are consistent with those described in the "Summary of Significant Accounting Policies."

Operating income includes all items except for interest income and expense. North American corporate expenses have not been allocated. Assets of geographic segments represent those assets identified with the operation of each segment.

(in thousands)	North America	Europe	Other	Consolidated
<b>August 31, 2002</b>				
Sales to unaffiliated customers	\$387,856	\$578,737	\$ —	\$ 966,593
Gross profit	\$ 54,176	\$106,157	\$ —	\$ 160,333
Operating income	\$ 2,639	\$ 58,504	\$ —	\$ 61,143
Interest expense, net	—	—	(3,562)	(3,562)
Income before taxes	\$ 2,639	\$ 58,504	\$(3,562)	\$ 57,581
Identifiable assets	\$266,923	\$345,409	\$ —	\$ 612,332
Depreciation expense	\$ 13,305	\$ 9,507	\$ —	\$ 22,812
Capital expenditures	\$ 9,309	\$ 17,456	\$ —	\$ 26,765
<b>August 31, 2001</b>				
Sales to unaffiliated customers	\$395,465	\$579,756	\$ —	\$ 975,221
Gross profit	\$ 41,854	\$ 91,411	\$ —	\$ 133,265
Operating income (loss)	\$ (7,310)	\$ 46,163	\$ —	\$ 38,853
Cost of plant closure - Akron, Ohio	—	—	(4,635)	(4,635)
Interest expense, net	—	—	(5,354)	(5,354)
Income (loss) before taxes	\$ (7,310)	\$ 46,163	\$(9,989)	\$ 28,864
Identifiable assets	\$258,249	\$320,422	\$ —	\$ 578,671
Depreciation expense	\$ 13,115	\$ 7,939	\$ —	\$ 21,054
Capital expenditures	\$ 11,484	\$ 21,890	\$ —	\$ 33,374
<b>August 31, 2000</b>				
Sales to unaffiliated customers	\$438,482	\$594,037	\$ —	\$1,032,519
Gross profit	\$ 61,041	\$106,122	\$ —	\$ 167,163
Operating income	\$ 14,429	\$ 58,336	\$ —	\$ 72,765
Interest expense, net	—	—	(4,666)	(4,666)
Income before taxes	\$ 14,429	\$ 58,336	\$(4,666)	\$ 68,099
Identifiable assets	\$297,790	\$275,100	\$ —	\$ 572,890
Depreciation expense	\$ 13,141	\$ 8,444	\$ —	\$ 21,585
Capital expenditures	\$ 16,416	\$ 16,036	\$ —	\$ 32,452

Below is a summary of sales point of origin and assets by location:

(in thousands)	2002	2001	2000
<b>Net Sales</b>			
United States	\$287,182	\$301,771	\$ 350,717
Germany	243,846	247,448	264,557
Other International	435,565	426,002	417,245
	\$966,593	\$975,221	\$1,032,519
<b>Long Lived Assets</b>			
United States	\$ 67,506	\$ 73,236	\$ 79,846
Other International	109,610	96,371	80,065
	\$177,116	\$169,607	\$ 159,911

The majority of the Company's sales for the year ended August 31, 2002 can be classified into four primary product families. The approximate percentage of consolidated sales for these product families is as follows:

	2002
Color and additive concentrates	38%
Polyolefins	24
Engineered compounds	24
Polyvinyl chloride (PVC)	6
Other	8
	100%

### Note 13 — Contingencies

The Company is engaged in various legal proceedings arising in the ordinary course of business. The ultimate outcome of these proceedings is not expected to have a material adverse effect on the Company's financial condition.

### Note 14 — Quarterly Financial Highlights (Unaudited)

(In thousands, except per share data)

	Quarter ended				Year ended
	Nov. 30, 2001	Feb. 28, 2002	May 31, 2002	Aug. 31, 2002	Aug. 31, 2002
Net Sales	\$238,148	\$213,554	\$259,617	\$255,274	\$966,593
Gross Profit	35,689	31,759	47,872	45,013	160,333
Net Income	5,210	4,457	11,704	10,783	32,154
Earnings Per Share of Common Stock:					
Basic	\$ .18	\$ .15	\$ .40	\$ .37	\$ 1.10
Diluted	\$ .18	\$ .15	\$ .39	\$ .36	\$ 1.08

  

	Quarter ended				Year ended
	Nov. 30, 2000	Feb. 28, 2001	May 31, 2001	Aug. 31, 2001	Aug. 31, 2001
Net Sales	\$256,616	\$238,873	\$252,588	\$227,144	\$975,221
Gross Profit	35,542	29,625	34,701	33,397	133,265
Net Income (Loss) <sup>(a)</sup>	(727)	1,422	6,486	5,511	12,692
Basic and Diluted Earnings Per Share of Common Stock:	\$ (.03)	\$ .05	\$ .22	\$ .19	\$ .43

<sup>(a)</sup> Net income for the quarter ended November 30, 2000 included a one-time charge of \$4,635,000 or \$.16 per share for costs relating to the closing of the Akron, Ohio facility.

**Notes to Consolidated Financial Statements**

**Note 15 — Interest and Other Income**

Interest and other income for the year ended August 31, 2000, includes \$2,689,000 in North America from consideration received due to the demutualization of an insurance carrier and \$1,211,000 from the settlement of an insurance claim resulting from equipment problems at a facility in North America. Net income includes \$2,535,000 or \$.07 per share related to these events.

**Note 16 — Akron Plant Closing**

During the first quarter of fiscal 2001, the Company announced its plan to terminate manufacturing at its plant in Akron, Ohio. Manufacturing was terminated as of December 31, 2000. As a result, the Company recorded a one-time, pre-tax charge of \$4,635,000, net of a curtailment gain of \$2,011,000, in the quarter ended November 30, 2000, of which \$1,035,000 related to employee severance costs and the balance was other exit costs. The charge was primarily non-cash and included the write-off of equipment to be scrapped and other assets related to the manufacturing operations and employee severance costs for 85 hourly and 33 salaried employees. The severance costs included mainly pension benefits, post-retirement adjustments and medical insurance. The curtailment gain of \$2,011,000 represents the gain realized from a reduction of the post-retirement benefit obligation due to the workforce reductions. The Company's plan for the closing of this facility was completed at May 31, 2002.

**Note 17 — Accumulated Other Comprehensive Income**

The components of Accumulated Other Comprehensive Income are as follows:

	2002	2001
Foreign currency translation	\$31,028,000	\$44,768,000
Minimum pension liability adjustment	202,000	177,000
	<u>\$31,230,000</u>	<u>\$44,945,000</u>

**Report of Independent Accountants**

[PricewaterhouseCoopers Logo]

**To the Board of Directors and Stockholders  
of A. Schulman, Inc.**

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income, stockholders' equity and cash flows present fairly, in all material respects, the financial position of A. Schulman, Inc. and its subsidiaries at August 31, 2002 and 2001, and the results of their operations and their cash flows for each of the three years in the period ended August 31, 2002, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

/s/ PricewaterhouseCoopers LLP

Cleveland, Ohio  
October 14, 2002

A. Schulman, Inc.  
**Management's Discussion and Analysis of  
Financial Condition and the Results of Operations**

**Results of Operations  
2002**

Net sales for 2002 were \$966.6 million, a decrease of 0.9% from sales of \$975.2 million for the comparable period in 2001. A comparison of net sales by business segment is as follows:

Sales	(in thousands)		
	2002	2001	Decrease
North America	\$387,856	\$395,465	\$(7,609)
Europe	578,737	579,756	(1,019)
	\$966,593	\$975,221	\$(8,628)

The two largest markets served by the Company are the packaging and automotive markets. For the year ended August 31, 2002, approximately 38% of net sales were derived from the packaging market. Net sales to the automotive market accounted for approximately 28% in the year ended August 31, 2002.

The majority of the Company's sales for 2002 can be classified into four primary product families. The approximate percentage of consolidated sales for these product families is as follows:

Product Family	Percent of Sales for 2002
Color and additive concentrates	38%
Polyolefins	24
Engineered compounds	24
Polyvinyl chloride (PVC)	6
Other	8
	100%

The translation effect of foreign currencies, primarily the strong euro, increased sales by \$15.9 million in 2002.

The reasons for the percentage change in 2002 sales are as follows:

	Increase (Decrease)
Tonnage	3.2%
Translation effect	1.6
Price/Mix	(5.7)
Percentage change in sales	(0.9)%

Tonnage increased 3.4% in Europe primarily due to capacity additions from new equipment in France and Germany. Tonnage was up 2.8% in North America due to the strength of the automotive industry and better capacity utilization.

A comparison of gross profit dollars and percentages by business segment for 2002 and 2001 is as follows:

Gross profit \$	(in thousands)			
	2002	2001	Increase	
			\$	%
Europe	\$106,157	\$ 91,411	\$14,746	16.1
North America	54,176	41,854	12,322	29.4
	\$160,333	\$133,265	\$27,068	20.3
Gross profit %	2002	2001		
Europe	18.3	15.8		
North America	14.0	10.6		
	16.6	13.7		

The increase in gross profits for 2002 was due to lower material costs, higher volume and an improvement in capacity utilization in North America.

A comparison of capacity utilization levels is as follows:

	2002	2001
Europe	87%	91%
North America	83%	81%
Worldwide	85%	86%

Tonnage was up for the year, but European capacity utilization declined, primarily due to the addition of four new manufacturing lines in 2002. These four lines increased European capacity by approximately 79 million pounds annually. Most of these lines commenced operation during the last half of the fiscal year. North American utilization was higher due to an increase in sales and a reduction in capacity after the closing of the Akron manufacturing facility in 2001.

A comparison of operating income (loss) by business segment for the year 2002 and 2001 is as follows:

	(in thousands)		
	2002	2001	Increase
Operating income (loss):			
Europe	\$58,504	\$46,163	\$12,341
North America	2,639	(7,310)	9,949
Cost of plant closure	—	(4,635)	4,635
Interest expense, net	(3,562)	(5,354)	1,792
	<u>\$57,581</u>	<u>\$28,864</u>	<u>\$28,717</u>

The operating income improvement in Europe and North America was due to higher profit margins, an increase in tonnage compared to 2001 and the positive impact of currency, primarily the euro. The margins were higher due to lower plastic resin prices, strong production levels at the manufacturing facilities and an increase in capacity utilization in North America.

Selling, general and administrative expenses for 2002 was up \$3.1 million or 3.3% compared to 2001. The increase is due to higher compensation and the translation effect of foreign currencies, which increased expenses by \$1.4 million for 2002.

Interest expense decreased in 2002 mainly due to lower interest rates. There was also a lower level of borrowings near the end of the fiscal year.

Foreign currency transaction losses were primarily due to changes in the value of currencies in major areas where the Company operates. The major portion of the losses in 2002 relates to changes in the value of the U.S. dollar compared with the Canadian dollar and the euro.

Minority interest represents a 30% equity position of Mitsubishi Chemical MKV Company in a partnership with the Company and a 35% equity position of P.T. Prima Polycon Indah in an Indonesian joint venture with the Company.

The effective tax rate decreased to 44.2% from 56.0% in 2001. The effective tax rate of 44.2% in 2002 is greater than the statutory rate of 35% primarily because no tax benefit has been recognized on losses in the United States. The fiscal 2001 effective tax rate was higher than in 2002 due to the \$4.6 million provision for the closing of the Akron plant in 2001 and a reduction in U.S. losses during fiscal 2002.

The translation effect of foreign currencies increased net income in 2002 by \$1.1 million or \$.04 per share for the year ended August 31, 2002.

**Management's Discussion and Analysis of  
Financial Condition and the Results of Operations**

Fiscal 2002 was a better year and reflected the positive results of actions over the last few years. Product lines have been rationalized, manufacturing lines of certain products were consolidated and expenditures have been controlled. The Company's business systems are providing benefits and serving customers on a timely and efficient basis throughout the world. The Company has continued to invest worldwide in order to meet customers' needs in the growing global market and has the cash flow necessary to finance future expansions. In addition, the strong financial condition of the Company provides the capability to meet new and challenging demands of the market.

Business continues to be quite good in the international operations, particularly Europe. Although there has been some moderation of growth in these economies, there continues to be good demand and a solid level of orders for the Company's products.

In the latter part of the fiscal 2002 fourth quarter, there was some softening of orders in North America. There has also been weaker than anticipated sales in September and early October. Although there is some concern about these current conditions in North America, the Company's plan provides for improved results for the 2003 fiscal year. The new fiscal year will bring many new challenges, but the Company is confident that the actions that were taken by management have positioned the organization to achieve continuing gains in the years ahead.

**2001**

Net sales for 2001 were \$975.2 million, down 5.5% from 2000 sales of \$1,032.5 million. A comparison of net sales is as follows:

Sales	(in thousands)		
	2001	2000	Decrease
North America	\$395,465	\$ 438,482	\$(43,017)
Europe	579,756	594,037	(14,281)
	<u>\$975,221</u>	<u>\$1,032,519</u>	<u>\$(57,298)</u>

The translation effect, primarily from the weaker euro, decreased 2001 sales by \$51.6 million.

Worldwide tonnage was 2.8% lower than in 2000. Tonnage was up 4.6% in Europe and down approximately 13.1% in North America. Tonnage was down in North America primarily due to lower sales to customers serving the North American automotive market and the closure of the Akron, Ohio manufacturing plant in December 2000. Additionally, major customers reduced their overall inventory balances in response to declining order levels and in anticipation of potentially lower prices.

Gross profit margins on sales were 13.7% in 2001 and 16.2% in 2000. A comparison of gross profit is as follows:

Gross Profit \$	(in thousands)			
	2001	2000	Decrease	
			\$	%
North America	\$ 41,854	\$ 61,041	\$(19,187)	(31.4)
Europe	91,411	106,122	(14,711)	(13.9)
	<u>\$133,265</u>	<u>\$167,163</u>	<u>\$(33,898)</u>	<u>(20.3)</u>
Gross Profit %			2001	2000
North America			10.6	13.9
Europe			15.8	17.9
			<u>13.7</u>	<u>16.2</u>

The decrease in gross profit in 2001 was due primarily to competitive price pressures and lower plant utilization.

A comparison of capacity utilization levels is as follows:

	2001	2000
North America	81%	86%
Europe	91%	86%
Worldwide	86%	86%

The decrease in North American capacity utilization was mainly due to lower sales to the automobile industry and reductions by customers in response to softer order levels and in anticipation of lower prices. European utilization was higher because of strong demand for concentrates and engineered products and high-volume products with lower margins.

Selling, general and administrative expenses decreased \$3.4 million in 2001. The translation effect, primarily from the weak euro, decreased these expenses by \$4.3 million, which offset increases in Europe. The remainder of the decrease is attributable to North American cost reductions implemented in 2001.

Interest expense was up in 2001 due to increased levels of borrowings.

Foreign currency transaction gains were primarily due to changes in the value of currencies in major areas where the Company operates. The major portion of the gains in 2001 relate to changes in the value of the U.S. dollar compared with the Canadian dollar and the euro.

Minority interest represents a 30% equity position of Mitsubishi Chemical MKV Company in a partnership with the Company and a 35% equity position of P.T. Prima Polycon Indah in an Indonesian joint venture with the Company.

During the first quarter of fiscal 2001, the Company announced its plan to terminate manufacturing at its plant in Akron, Ohio. Manufacturing was terminated as of December 31, 2000. As a result, the Company recorded a one-time, pre-tax charge of \$4,635,000 in the quarter ended November 30, 2000, of which \$1,035,000 related to employee severance costs and the balance was other exit costs. The charge was primarily non-cash and included the write-off of equipment to be scrapped and other assets related to the manufacturing operations and employee severance costs for 85 hourly and 33 salaried employees. The severance costs included mainly pension benefits, post-retirement adjustments and medical insurance. At August 31, 2001, the Company had remaining reserves of \$193,000 related to cash out-flows primarily for employee severance costs, which were expected to be paid during the next three months. The Company's plan for the closing of this facility was completed at May 31, 2002.

The effective tax rate increased to 56.0% in 2001 from 44.6% in 2000. The 2001 effective rate is greater than the statutory rate of 35% primarily because of the \$4,635,000 provision for the closing of the Akron, Ohio plant and losses in the United States. No tax benefit has been recognized on losses in the United States.

The translation effect of currencies, primarily from the weaker euro, decreased net income by approximately \$2.5 million or \$.08 per share in 2001.

North American operating income was down \$21.7 million for the year because of a reduction of \$19.2 million in gross profits due to lower sales volumes, a reduction in plant utilization, and continuing competitive price pressures.

The adverse translation effects of the euro and a \$14.7 million reduction in gross profit from fiscal 2000 were the major reasons for the decline of \$12.2 million in European operating income. The reductions in European gross profits were the result of continuing competitive pricing pressures.

## Critical Accounting Policies

The Company has identified critical accounting policies that, as a result of the judgments, uncertainties, and the operations involved, could result in material changes to its financial condition or results of operations under different conditions or using different assumptions. The Company's most critical accounting policies relate to the allowance for doubtful accounts, inventory reserves and interim provisions for income taxes.

Management records an allowance for doubtful accounts receivable based on the careful monitoring of the current and projected credit quality of the Company's customers, historical experience, customer payment history, expected trends and other factors that affect collectibility. Changes in these factors or changes in economic circumstances could result in changes to the allowance for doubtful accounts.

Management establishes an inventory reserve based on historical experience and amounts expected to be realized for slow-moving and obsolete inventory. The Company monitors its slow-moving and obsolete inventory on a quarterly basis and makes adjustments as considered necessary. The proceeds from the sale or dispositions of these inventories may differ from the net recorded amount.

The Company's quarterly provision for income taxes involves a significant amount of judgment by management. Quarterly, the provision for income taxes is based upon actual year to date results plus an estimate of pretax income for the remainder of the year. This provision is impacted by the income and tax rates of the countries where the Company operates. A change in the geographical source of the Company's income can have a significant effect on the tax rate.

## Liquidity and Capital Resources

	(in millions)		
	August 31, 2002	August 31, 2001	% Change
Cash and cash equivalents	\$ 64.0	\$ 52.6	21.7%
Working capital	301.0	289.3	4.0
Long-term debt	81.0	105.4	(23.1)
Stockholders' equity	356.4	322.1	10.6

The Company's cash and cash equivalents increased \$11.4 million, or 21.7%, from August 31, 2001. The cash increase was derived primarily from cash provided from operations amounting to \$70.5 million less capital expenditures of \$26.8 million, cash dividends of \$16.0 million and a reduction of long-term debt amounting to \$24.4 million. Cash generated from operating activities increased from last year due to an improvement in both European and North American operating income.

During fiscal 2002, management repatriated approximately \$26.0 million as dividends from its foreign subsidiaries. This cash was used to repay long-term debt and for other working capital requirements.

Capital expenditures were \$26.8 million for the year ended August 31, 2002 compared with \$33.4 million in the comparable period last year. The largest amount of capital expenditures occurred in Germany, France, Belgium, Italy and Mexico primarily for the addition of manufacturing lines, enhancements to existing equipment, and the addition of plant and warehouse space. The Company anticipates capital expenditures for fiscal 2003 will be approximately \$25.0 million, depending on the progress of each project.

The Company reduced long-term debt by \$24.4 million, primarily due to cash flow from operations. Total long-term debt as of August 31, 2002 was \$81.0 million.

As of August 31, 2002, the current ratio was 3.5:1 and working capital was \$301.0 million. Accounts receivable increased \$10.2 million from the year ended August 31, 2001. Accounts receivable was higher at August 31, 2002 compared with 2001 primarily because of the translation effect of foreign currencies, which increased receivables by \$5.9 million, and higher fourth quarter sales in 2002 compared with 2001.

The ratio of long-term liabilities to capital was 25.9% at August 31, 2002 and 31.0% at August 31, 2001. This ratio is calculated by dividing the sum of long-term debt and other long-term liabilities by the sum total of total stockholders' equity, long-term debt and other long-term liabilities. The primary factor contributing to the decrease of this ratio was a decline of \$24.4 million in borrowings.

On October 2, 2001, the Company established a new four-year \$130,000,000 revolving credit agreement, replacing a \$100,000,000 facility in place at August 31, 2001. Under terms of the new agreement, the Company is required to satisfy certain financial and operating covenants including leverage ratio, interest coverage ratio and capitalization ratio. The revolving credit agreement is unsecured.

The Company has an outstanding private placement agreement of \$50,000,000 of Senior Notes due in 2009. The interest rate is fixed at 7.27% and is payable quarterly with principal due upon maturity in 2009. In 1999, the Company completed an interest rate lock in order to reduce the interest cost over the life of the notes. Proceeds from this transaction totaling \$630,000 have been deferred and will be amortized over the life of the loan, effectively reducing the annual interest rate from 7.27% to 7.14%. Under this agreement, as of August 31, 2002, approximately \$44.0 million of retained earnings was available for the payment of cash dividends. The Company's year-end review of the covenants under these agreements indicates no defaults or any non-compliance with their covenants.

The Company's unfunded pension liability is approximately \$27.0 million at August 31, 2002. This amount is primarily due to an unfunded plan of \$23.1 million maintained by the Company's German subsidiary. Under this plan, there is no separate vehicle to accumulate assets to provide for the payment of benefits. The benefits are paid directly by the Company to the participants. It is anticipated that the German subsidiary will generate sufficient funds from operations to pay these benefits in the future.

The Company enters into forward foreign exchange contracts as a hedge against amounts due or payable in foreign currencies. These contracts limit the Company's exposure to fluctuations in foreign currency exchange rates. Any gains or losses associated with these contracts as well as the offsetting gains or losses from the underlying assets or liabilities hedged are recognized on the foreign currency transaction line in the Consolidated Statement of Income. The Company estimates that a 10% change in foreign exchange rates at August 31, 2002 would have changed the fair value of the contracts by approximately \$1.6 million. Changes in the fair value of forward exchange contracts are substantially offset by changes in the fair value of the hedged positions. The Company does not hold or issue

financial instruments for trading purposes or utilize any other types of derivative instruments.

The Company leases certain land and buildings for its European segment under a capital lease. The total amount due on this capital lease at August 31, 2002 is \$1,151,000.

A. Schulman, Inc.

## Management's Discussion and Analysis of Financial Condition and the Results of Operations

Aggregate maturities of long-term debt (including capital lease obligations) subsequent to August 31, 2002 are presented below:

Fiscal	2004	\$ 413,000
	2005	30,337,000
	2006	288,000
	2009	50,000,000
Total		\$81,038,000

Operating lease information is provided in the footnotes of the Company's Annual Report. The aggregate future minimum rental commitment for non-cancelable leases, excluding obligations for taxes, insurance, etc. was \$6.5 million at August 31, 2002.

The Company's outstanding commercial commitments at August 31, 2002 are not material to the Company's financial position, liquidity or results of operations.

The Company has declared and paid four quarterly cash dividends of \$.135 per share during fiscal 2002. The total amount of these payments aggregated \$16.0 million. Cash flow from operations has been sufficient to fund the payment of these dividends.

During the year ended August 31, 2002, the Company did not repurchase any shares of its common stock. Approximately 1.7 million shares remain under a 6 million-share authorization approved by the Board of Directors in August 1998. The Company may repurchase additional common stock in fiscal year 2003 subject to market conditions. For the year ended August 31, 2002, 206,000 common shares were issued upon the exercise of employee stock options. The total amount received from the exercise of these options was \$3.6 million.

The assets and liabilities of the Company's foreign subsidiaries are translated into U.S. dollars using current exchange rates. Income statement items are translated at average exchange rates prevailing during the period. The resulting translation adjustments are recorded in the "accumulated other comprehensive income" account in stockholders' equity. The weakening of the U.S. dollar during the year ended August 31, 2002 increased this account by \$13.7 million.

### New Accounting Pronouncements

On September 1, 2001 the Company adopted the provisions of SFAS No. 141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets." SFAS No. 141 requires that all business combinations be accounted for by the purchase method and that certain acquired intangible assets be recognized as assets apart from goodwill. SFAS No. 142 provides that goodwill should not be amortized but instead be tested for impairment annually at the reporting unit level. In accordance with SFAS No. 142, the Company completed a transitional goodwill impairment test during the quarter ended February 28, 2002, which resulted in no impairment loss being recognized upon adoption. The Company also conducts a formal impairment test of goodwill at the reporting unit level on an annual basis and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying value. The annual test resulted in no impairment. Goodwill and intangible assets were reclassified from deferred charges for all reportable periods.

In June 2001, the Financial Accounting Standards Board (the FASB) issued SFAS No. 143, "Accounting for Asset Retirement Obligations" (SFAS 143), which addresses the recognition and remeasurement of obligations associated with the retirement of tangible long-lived assets and the associated asset retirement cost. The provisions of SFAS 143 were adopted by the Company effective September 1, 2002. The adoption of SFAS 143 did not have a material impact on the Company's financial position or results of operations.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (SFAS 144), which addresses financial accounting and reporting for the impairment or disposal of long-lived assets. SFAS 144 applies to all long-lived assets, including discontinued operations, and develops one accounting model for long-lived assets to be disposed of by sale. This Statement supersedes SFAS No. 121, "Accounting for the Impairment of Long-lived Assets and for Long-lived Assets to be Disposed Of" (SFAS 121) and the accounting and reporting provisions of APB No. 30, "Reporting the Results of Operations — Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions" (APB 30), for the disposal of a segment of a business. The provisions of SFAS 144 were adopted by the Company effective September 1, 2002. The adoption of SFAS 144 did not have a material impact on the Company's financial position or results of operations.

In July 2002, the FASB issued SFAS No. 146 (SFAS 146), "Accounting for Costs Associated with Exit or Disposal Activities." SFAS 146 requires that a liability for a cost associated with an exit or disposal activity be recognized when the liability is incurred and establishes that fair value is the objective for initial measurement of the liability. This statement is effective for exit or disposal activities initiated after December 31, 2002. The Company does not expect the adoption of SFAS 146 to have a material impact on its financial position or results of operations.

### Cautionary Statements

Statements in this report which are not historical facts are forward-looking statements which involve risks and uncertainties and actual events or results could differ materially from those expressed or implied in this report. These "forward-looking statements" are based on currently available information. They are also inherently uncertain, and investors must recognize that events could turn out to be significantly different from what we had expected. Examples of such uncertainties include, but are not limited to, the following:

- Worldwide and regional economic, business and political conditions
- Fluctuations in the value of currencies in major areas where the Company operates, i.e. the U.S. dollar, euro, U.K. pound sterling, Canadian dollar, Mexican peso and Indonesian rupiah, etc.
- Fluctuations in prices of plastic resins and other raw materials
- Changes in customer demand and requirements

#### **Quantitative and Qualitative Disclosure about Market Risk**

The Company enters into forward exchange contracts to reduce its exposure to fluctuations in related foreign currencies. These contracts are with major financial institutions and the risk of loss is considered remote. The total value of open contracts and any risk to the Company as a result of these arrangements is not material to the Company's financial position, liquidity or results of operations.

**Six-Year Summary of Selected Financial Data****(In thousands, except per share data)**

	Year Ended August 31,					
	2002	2001	2000	1999	1998	1997
Net sales	\$ 966,593	\$ 975,221	\$ 1,032,519	\$ 985,623	\$ 993,394	\$ 996,376
Interest and other income	2,179	1,969	6,703 <sup>(2)</sup>	2,712	3,072	4,998
	968,772	977,190	1,039,222	988,335	996,466	1,001,374
Cost of sales	806,260	846,592	865,357	805,030	823,856	833,345
Other costs, expenses, etc	104,931	101,734	105,766	105,349	86,281	81,747
	911,191	948,326	971,123	910,379	910,137	915,092
Income before taxes and cumulative effect of accounting changes	57,581	28,864	68,099	77,956	86,329	86,282
Provision for U.S. and foreign income taxes	25,427	16,172	30,395	30,167	34,179	35,538
Income before cumulative effect of accounting changes	32,154	12,692	37,704	47,789	52,150	50,744
Cumulative effect of accounting changes <sup>(3)</sup>	—	—	—	—	(2,007)	—
Net income	\$ 32,154	\$ 12,692 <sup>(1)</sup>	\$ 37,704	\$ 47,789	\$ 50,143	\$ 50,744
Total assets	\$ 612,332	\$ 578,671	\$ 572,890	\$ 591,527	\$ 561,920	\$ 562,945
Long-term debt	\$ 81,038	\$ 105,415	\$ 83,638	\$ 65,000	\$ 40,000	\$ 12,009
Total stockholders' equity	\$ 356,361	\$ 322,079	\$ 323,461	\$ 356,246	\$ 366,271	\$ 393,401
Average number of common shares outstanding, net of treasury shares:						
Basic	29,296,435	29,184,605	30,224,433	31,671,768	35,236,098	37,125,345
Diluted	29,667,037	29,199,566	30,224,433	31,679,614	35,275,327	37,149,595
Diluted earnings per share:						
Before cumulative effect of accounting changes	\$ 1.08	\$ .43	\$ 1.25	\$ 1.51	\$ 1.48	\$ 1.37
Cumulative effect of accounting changes <sup>(3)</sup>	—	—	—	—	\$ (0.06)	—
Net income	\$ 1.08	\$ .43	\$ 1.25	\$ 1.51	\$ 1.42	\$ 1.37
Cash dividends per common share	\$ .54	\$ .54	\$ .53	\$ .49	\$ .45	\$ .41
Book value per common share	\$ 12.08	\$ 10.99	\$ 10.99	\$ 11.41	\$ 10.97	\$ 10.83

(1) Includes a charge of \$4,635,000 or \$.16 per share related to the cost of Akron, Ohio plant closure.

(2) Includes \$3,900,000 in North America from consideration received due to the demutualization of an insurance carrier and the settlement of an insurance claim resulting from equipment problems at a facility in North America. Net income includes \$2,535,000 or \$.07 per share related to these events.

(3) On November 20, 1997, The FASB Emerging Issues Task Force issued a new ruling which requires the write-off of business process re-engineering costs. Accordingly, \$3,237,000 of such costs capitalized as of August 31, 1997 were written off in the quarter ending November 30, 1997. This write-off, net of income taxes, amounted to \$2,007,000 or \$.06 per common share and was accounted for as a change in accounting.

A. Schulman, Inc.  
**Corporate Information**

**The Board of Directors**

**Robert A. Stefanko**  
Chairman

**Terry L. Haines**  
President and Chief Executive Officer

**Joseph M. Gingo**  
Senior Vice President,  
Technology and Global Products Planning,  
The Goodyear Tire and Rubber Company

**Willard R. Holland**  
Former Chairman,  
FirstEnergy Corp.

**James A. Karman**  
Former Vice Chairman, RPM, Inc.

**James S. Marlen**  
Chairman, President and Chief Executive Officer,  
Ameron International Corporation

**Dr. Peggy Gordon Miller**  
President,  
South Dakota State University

**Dr. Paul Craig Roberts**  
Chairman,  
The Institute for Political Economy

**Rene C. Rombouts**  
General Manager-Europe

**John B. Yasinsky**  
Former Chairman,  
OMNOVA Solutions, Inc.

**Annual Meeting**  
of Stockholders will be held on  
Thursday, December 5, 2002, at 10 AM  
E.S.T., at the Hilton Inn West 3180 West  
Market Street Akron, Ohio 44333

**Independent Accountants**  
PricewaterhouseCoopers LLP  
BP Tower  
27th Floor  
200 Public Square  
Cleveland, Ohio 44114-2301

**Stock Listing**  
The common stock of  
A. Schulman, Inc. is traded  
and quoted through the  
NASDAQ National Market  
System. Symbol: SHLM

**Executive Officers**

**Terry L. Haines**  
President and Chief Executive Officer

**Robert A. Stefanko**  
Chairman, Chief Financial Officer and Treasurer

**Alain C. Adam**  
Vice President— International Automotive Operations

**Ronald G. Andres**  
Vice President— North American Manufacturing

**John M. Myles**  
Vice President— North American Purchasing

**Dr. Rengarajan Ramesh**  
Vice President— Technology

**Barry A. Rhodes**  
Vice President— North American Sales

**James H. Berick**  
Secretary

**European Operations**

**Rene C. Rombouts**  
General Manager— Europe

**Otto H. Bruder**  
Associate General Manager— Europe

**Jack B. Taylor**  
Associate General Manager— Europe

**Transfer Agent**

National City Bank  
Corporate Trust Operations  
P.O. Box 92301  
Cleveland, OH 44193-0900

Any questions regarding shareholder  
records should be directed to:

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800-622-6757  
E-mail address:  
shareholder.inquiries@nationalcity.com

**Corporate Headquarters**

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**Midwest Regional Sales Office**

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Schaumburg, IL 60173  
(847) 397-3973

**Western Regional Sales Office**

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Pasadena, CA 91106  
(626) 792-0053

**Technology Centers**

**A. Schulman, Inc.**  
Product Technology Center  
1183 Home Avenue  
Akron, Ohio 44310  
(330) 630-3315

**A. Schulman, Inc.**

Color Technology Center  
1475 Wolf Creek Trail  
Sharon Center, Ohio 44274  
(330) 239-0101

The annual report to the Securities  
and Exchange Commission,  
Form 10-K, will be made available  
upon request without charge.

Write:

Robert A. Stefanko,  
Chairman and Chief Financial Officer  
A. Schulman, Inc.  
3550 West Market Street  
Akron, Ohio 44333

## Foreign Offices

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### Paris, France

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Immeuble Dynasteur  
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San Pedro Garza Garcia,  
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### San Luis Potosi, Mexico

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## Representative Offices

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## Plants

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350 North Buckeye Street  
(419) 483-2931

### Orange, Texas 77630

(Dispersion Plant)  
3007 Burnett  
(409) 883-9371

### Sharon Center, Ohio 44274

(Specialty Compounding Division)  
1475 Wolf Creek Trail  
(330) 239-0101

### Nashville, Tennessee 37211-3333

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### Orange, Texas 77632

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[A. SCHULMAN LOGO]

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