OMNOVA SOLUTIONS INC
Form 10-Q
June 29, 2007
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SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarter Ended May 31, 2007	**Commission File Number 1-15147**

OMNOVA Solutions Inc.

(Exact name of registrant as specified in its charter)

Ohio	**34-1897652**
(State of Incorporation)	**(I.R.S. Employer Identification No.)**

175 Ghent Road Fairlawn, Ohio 44333-3300

(Address of principal executive offices) (Zip Code)

Registrant s telephone number, including area code (330) 869-4200

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer ¨ Accelerated filer x Non-accelerated filer ¨

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

At May 31, 2007, there were 42,135,145 outstanding shares of OMNOVA Solutions Common Stock, par value $0.10.

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Part I. Financial Information

Item 1. Financial Statements

OMNOVA SOLUTIONS INC.

Consolidated Statements of Operations

(Dollars in Millions, Except Per Share Data)

(Unaudited)

	Three Months Ended May 31,		Six Months Ended May 31,	
	2007	**2006**	**2007**	**2006**
Net Sales	**$ 188.0**	$ 177.8	**$ 352.8**	$ 347.6
Costs and Expenses				
Cost of goods sold	**150.9**	136.9	**285.6**	272.6
Selling, general and administrative	**25.2**	26.6	**50.5**	52.7
Depreciation and amortization	**5.4**	5.3	**10.6**	10.6
Restructuring and severance	**.1**		**.4**	
Interest expense	**4.6**	5.2	**9.3**	10.4
Equity earnings in affiliates, net	**(.6)**	(1.2)	**(.7)**	(1.5)
Debt redemption expense	**12.4**		**12.4**	
Other income, net	**(.2)**	(.2)	**(.4)**	
	197.8	172.6	**367.7**	344.8
Income (loss) from continuing operations before income taxes	**(9.8)**	5.2	**(14.9)**	2.8
Income tax expense		.1		.1
Income (loss) from continuing operations	**(9.8)**	5.1	**(14.9)**	2.7
Discontinued operation, net of tax:				
Income (loss) from operations		.2		(1.7)
Net Income (Loss)	**$ (9.8)**	$ 5.3	**$ (14.9)**	$ 1.0
Basic and Diluted Income (Loss) Per Share				
Income (loss) from continuing operations	**$ (.23)**	$ .13	**$ (.36)**	$ .06
Income (loss) from discontinued operations				(.04)
Net Income (Loss)	**$ (.23)**	$ .13	**$ (.36)**	$ .02

See notes to the unaudited interim consolidated financial statements.

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OMNOVA SOLUTIONS INC.

Consolidated Balance Sheets

(Dollars in Millions, Except Per Share Amounts)

	May 31, 2007 (Unaudited)	November 30, 2006
ASSETS:		
Current Assets		
Cash and cash equivalents	$ 13.6	$ 26.4
Restricted cash	3.4	
Accounts receivable, net	99.4	94.4
Inventories	41.4	33.4
Prepaid expenses and other	4.7	3.3
Deferred income taxes	.3	.3
Total Current Assets	162.8	157.8
Restricted cash		12.3
Property, plant and equipment	454.3	448.2
Accumulated depreciation	(319.0)	(309.7)
	135.3	138.5
Trademarks and other intangible assets, net	5.0	5.7
Investment in affiliates	20.8	19.1
Other assets	4.8	5.5
Total Assets	$ 328.7	$ 338.9
LIABILITIES AND SHAREHOLDERS EQUITY:		
Current Liabilities		
Short-term debt	$ 4.5	$
Accounts payable	66.2	58.2
Accrued payroll and personal property taxes	11.5	14.2
Accrued interest	.5	9.3
Employee benefit obligations	5.0	5.1
Other current liabilities	5.2	6.7
Total Current Liabilities	92.9	93.5
Long-term debt	168.5	165.0
Postretirement benefits other than pensions	10.8	17.1
Pension liability	5.6	3.0
Other liabilities	9.3	11.5
Deferred income taxes	.3	.3
Total Liabilities	287.4	290.4
Shareholders Equity		
Preference stock - $1.00 par value; 15 million shares authorized; none outstanding		
Common stock - $0.10 par value; 135 million shares authorized; 43.1 million shares issued as of May 31, 2007 and November 30, 2006	4.3	4.3
Additional contributed capital	314.3	313.8

Retained deficit		**(251.5)**		(236.6)
Treasury stock at cost; .9 million and 1.1 million shares as of May 31, 2007 and November 30, 2006, respectively		**(7.5)**		(8.4)
Accumulated other comprehensive loss		**(18.3)**		(24.6)
Total Shareholders Equity		**41.3**		48.5
Total Liabilities and Shareholders Equity	**$**	**328.7**	$	338.9

See notes to the unaudited interim consolidated financial statements.

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OMNOVA SOLUTIONS INC.

Consolidated Statements of Cash Flows

(Dollars in Millions)

(Unaudited)

	Six Months Ended May 31, 2007	Six Months Ended May 31, 2006
Operating Activities		
Net income (loss)	**$ (14.9)**	$ 1.0
Income (loss) from discontinued operations		1.7
Income (loss) from continuing operations	**(14.9)**	2.7
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Equity earnings in affiliates	**(.7)**	(1.5)
Depreciation, amortization and (gain) loss on sale of fixed assets	**10.5**	10.6
Debt redemption expense	**12.4**	
Non-cash stock compensation expense	**.4**	.4
Other	**1.9**	.4
Changes in operating assets and liabilities:		
Current assets	**(15.4)**	(9.1)
Current liabilities	**(4.9)**	(5.6)
Other non-current assets	**1.3**	(1.6)
Other non-current liabilities	**(1.2)**	1.8
Discontinued operations		(.7)
Net Cash (Used) In Operating Activities	**(10.6)**	(2.6)
Investing Activities		
Capital expenditures	**(6.1)**	(3.7)
Proceeds from restricted cash	**12.3**	
Discontinued operations		(.5)
Net Cash Provided By (Used) In Investing Activities	**6.2**	(4.2)
Financing Activities		
Long-term debt incurred	**392.7**	391.6
Long-term debt paid	**(389.2)**	(383.0)
Net short-term debt proceeds	**4.5**	
Cash paid for debt redemption expense and refinance costs	**(12.0)**	
Deferred financing cost	**(2.6)**	
Restricted cash for debt redemption	**(3.4)**	
Other	**.2**	.7
Net Cash (Used) In Provided By Financing Activities	**(9.8)**	9.3
Effect of exchange rate changes on cash	**1.4**	2.8
Net (Decrease) Increase In Cash And Cash Equivalents	**(12.8)**	5.3
Cash and cash equivalents at beginning of period	**26.4**	9.9
Cash And Cash Equivalents At End Of Period	**$ 13.6**	$ 15.2

Supplemental Cash Flows Information		
Cash paid:		
Interest	**$ 18.3**	$ 10.3
Income taxes	**$**	$

See notes to the unaudited interim consolidated financial statements.

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OMNOVA SOLUTIONS INC.

NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

AS OF MAY 31, 2007

(In Millions of Dollars, Except Per Share Data)

Note A Basis of Presentation

The accompanying unaudited interim consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial statements and with the instructions to Form 10-Q and Article 10 of Regulation S-X and, therefore, do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. These interim statements should be read in conjunction with the financial statements and notes thereto included in the OMNOVA Solutions Inc. (OMNOVA Solutions or the Company) Annual Report on Form 10-K for the year ended November 30, 2006, previously filed with the Securities and Exchange Commission (SEC).

The balance sheet at November 30, 2006 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements.

These interim consolidated financial statements reflect all adjustments that are, in the opinion of management, necessary for a fair presentation of the results for the interim period and all such adjustments are of a normal recurring nature. The results of operations for the interim period are not necessarily indicative, if annualized, of those to be expected for the full year.

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

The Company has historically experienced stronger sales and income in its second, third and fourth quarters, comprised of the three-month periods ending May 31, August 31 and November 30. The Company s performance in the first quarter (December through February) has historically been weaker due to generally lower levels of customer manufacturing, refurbishment and construction over the holidays and cold weather months.

A detailed description of the Company s significant accounting policies and management judgments is located in the audited consolidated financial statements for the year ended November 30, 2006, included in the Company s Form 10-K filed with the Securities and Exchange Commission.

Segment operating profit represents net sales less applicable costs, expenses and provisions for restructuring, severance, asset write-offs and work stoppage costs relating to operations. Segment operating profit excludes unallocated corporate headquarters expenses, provisions for corporate headquarters restructuring and severance, interest expense and income taxes. Corporate headquarters expense includes the cost of providing and maintaining the corporate headquarters functions, including salaries, rent, travel, entertainment, depreciation, utility costs, outside services and amortization of deferred financing costs.

Certain reclassifications have been made to conform prior period information to the current presentation. In addition, the results of operations and cash flows of the Building Products business, previously a reportable operating segment, have been reported as discontinued operations for all periods presented. Unless otherwise indicated, all disclosures in the notes to the unaudited interim consolidated financial statements relate to the continuing operations of the Company.

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Note A Basis of Presentation (Continued)

New Accounting Pronouncements In July 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109. FIN 48 clarifies the accounting for uncertainty in income taxes recognized by prescribing a recognition threshold and measurement attribute for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for years beginning after December 15, 2006. This interpretation will be effective for the Company beginning in the first quarter of 2008. The Company is in the process of determining the impact of this Interpretation on the Company s consolidated financial statements.

In September 2006, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 157, Fair Value Measurements. SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. This Statement is effective for years beginning after November 15, 2007. The Company is in the process of determining the impact of this Statement on the Company s consolidated financial statements.

Effective November 30, 2006, the Company adopted the recognition provisions of SFAS No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R). This Statement requires employers to recognize in their balance sheets the overfunded or underfunded status of defined benefit post-retirement plans, measured as the difference between the fair value of plan assets and the benefit obligation (the projected benefit obligation for pension plans and the accumulated postretirement benefit obligation for other post-retirement plans). Employers must recognize the change in the funded status of the plan in the year in which the change occurs through other comprehensive income. This Statement also requires plan assets and obligations to be measured as of the employer s balance sheet date. The measurement provision of this Statement will be effective for years beginning after December 15, 2008, with early application encouraged. The Company has not yet adopted the measurement provisions of this Statement and is in the process of determining the impact of the adoption on the Company s consolidated financial statements.

Note B Restricted Cash

As a result of the Company s sale of its Building Products business, the Company placed $12.3 million of the proceeds from the sale into a restricted long-term cash account for the benefit of the Company s bondholders, which represented the fair value of the property, plant and equipment of the sold business that was previously pledged as collateral. The Company redeemed this restricted cash and interest in connection with its debt redemption and refinancing. As of May 31, 2007, the Company placed $3.4 million in a restricted cash account to redeem the remaining principal, premium and accrued interest of its remaining 11 $^{1}/4$% Senior Secured Notes outstanding.

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Note C Inventories

Inventories are stated at the lower of cost or market value. A portion of inventories is priced by use of the last-in, first-out (LIFO) method using various dollar value pools. An actual valuation of inventory under the LIFO method is made only at the end of each year based on the inventory levels and costs at that time. Accordingly, interim LIFO calculations are based on management s judgments of expected year-end inventory levels and costs and are subject to final year-end LIFO inventory valuations. The remaining portion of inventories are stated using the first-in, first-out (FIFO) method. Inventories valued using the LIFO method represented approximately 65% and 74% of the total replacement cost of inventories at May 31, 2007 and November 30, 2006, respectively. Components of inventory are as follows:

	May 31, 2007	November 30, 2006
Raw materials and supplies	**$ 18.9**	$ 18.1
Work-in-process	**3.8**	2.8
Finished products	**51.9**	46.4
Approximate replacement cost of inventories	**74.6**	67.3
LIFO reserves	**(24.5)**	(24.0)
Other reserves	**(8.7)**	(9.9)
Inventories	**$ 41.4**	$ 33.4

Note D Long-Term Debt and Credit Lines

On May 22, 2007, the Company entered into a $150 million Term Loan Credit Agreement (Term Loan) due May 2014. The Term Loan carries a variable interest rate based on, at the Company s option, either an alternate base rate or a eurodollar rate, in each case plus an applicable margin. The alternate base interest rate is a fluctuating rate equal to the higher of the Prime Rate or the sum of the Federal Funds Effective Rate plus 50 basis points. The applicable margin for the alternate base rate is 150 basis points. The eurodollar rate is a periodic fixed rate equal to the London Inter Bank Offered Rate (LIBOR). The applicable margin for the eurodollar rate is 250 basis points. Annual principal payments consists of $1.5 million, which are due in quarterly installments, and annual excess free cash flow payments as defined in the Term Loan agreement, with any remaining balance to be paid May 2014. The Company can prepay any amount at any time without penalty upon proper notice and subject to a minimum dollar requirement. The Term Loan is secured by all real property and equipment of the Company s domestic facilities and stock and equity investments of the Company s non-domestic subsidiaries. The Term Loan contains affirmative and negative covenants, including limitations on additional debt, certain investments and acquisitions outside of the Company s line of business. The Term Loan requires the Company to maintain a net leverage ratio of less than 5.5 to 1 and at May 31, 2007, the Company was in compliance with this requirement. The Term Loan also provides for additional borrowings of up to $75 million, provided that certain requirements are met including an interest coverage ratio and a senior secured leverage ratio.

Proceeds of the Term Loan, along with cash, restricted cash and other resources of the Company, were used to redeem $162 million of the Company s $165 million 11/4% Senior Secured Notes (Notes). In connection with the redemption of the Notes, the Company paid $9.8 million in premium and tender fees. Additionally, the Company wrote off $2.6 million of unamortized debt issuance costs which were being amortized over the term of the Notes. As of May 31, 2007, the Company placed an amount equal to the principal, premium and accrued interest in a restricted cash account to redeem the remaining Notes. The remaining $3.0 million of Notes were redeemed on June 22, 2007.

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Note D Long-Term Debt and Credit Lines (Continued)

On May 31, 2007, the Company entered into a fixed rate interest rate swap agreement totaling $50 million to convert a portion of the outstanding term loan from variable to fixed rates. Under this agreement, the Company will pay a fixed rate of 7.73% and receive a variable rate based on LIBOR plus a margin of 250 basis points. The variable rate is reset every three months, at which time the interest will be settled and will be recognized as adjustments to interest expense. This swap agreement is designated as a cash flow hedge, and as such, any resulting gain or loss on the derivative instrument will be recognized in accumulated other comprehensive income, until it is realized with a corresponding adjustment to long-term debt. The fair value of the swap as of May 31, 2007 was $0.

In connection with the Term Loan, on May 22, 2007 the Company amended its senior secured revolving credit facility (Facility). The Facility was increased to $80 million from $72 million and extended until May 2012. The Facility includes a $15 million sublimit for the issuance of commercial and standby letters of credit and a $10 million sublimit for swingline loans. Borrowings under the Facility are limited to a borrowing base using customary advance rates for eligible accounts receivable and inventory. Borrowings under the Facility are secured by domestic accounts receivable, inventory and intangible assets. The Facility contains affirmative and negative covenants, similar to the Term Loan, including limitations on additional debt, certain investments and acquisitions outside of the Company s line of business. If the average excess availability of the Facility falls below $20 million, the Company must maintain a fixed charge coverage ratio greater than 1.1 to 1 as defined in the agreement. The Company may request an increase in available borrowings under the Facility of up to $20 million (for a maximum of $100 million) upon satisfaction of certain requirements.

Advances under the Facility bear interest, at the Company s option, at either an alternate base rate or a eurodollar rate, in each case plus an applicable margin. The alternate base interest rate is a fluctuating rate equal to the higher of the Prime Rate or the sum of the Federal Funds Effective Rate plus 50 basis points. The applicable margin for the alternate base rate will vary from 0.0% to 0.25% depending on the Company s fixed charge coverage ratio and the margin was 0.0% at May 31, 2007. The eurodollar rate is a periodic fixed rate equal to LIBOR. The applicable margin for the eurodollar rate will vary from 1.25% to 2.0% depending on the Company s fixed charge coverage ratio and the margin was 1.5% at May 31, 2007.

The Facility requires a commitment fee based on the unused portion of the Facility. The commitment fee will vary from 0.125% to 0.25% based on the Company s fixed charge coverage ratio and was 0.125% at May 31, 2007.

At May 31, 2007, the available balance under the Facility, net of outstanding letters of credit and required reserves was $56.6 million. Borrowings under the Facility were $20.0 million and standby letters of credit outstanding were $3.4 million as of May 31, 2007.

Note E Discontinued Operations

On September 27, 2006, the Company sold substantially all of the assets and liabilities of the Building Products business to BFS Diversified Products, LLC, for $25.9 million in cash resulting in a gain of $18.2 million. No income taxes were provided due to the utilization of the Company s net operating loss carryforwards. The Company retained $10.5 million of Building Products trade accounts receivable, all of which were collected as of November 30, 2006.

In accordance with the provisions of SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, the results of operations and cash flows of the Building Products business for all periods presented have been reported as discontinued operations. This transaction allows the Company to focus its resources on its strategic product lines with strong market positions and will provide the Company with flexibility to grow its remaining segments.

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Note E Discontinued Operations (Continued)

The results of operations for the three and six months ended May 31, 2006 for the Building Products business reported as discontinued operations were:

(Dollars in millions)	Three Months Ended May 31, 2006	Six Months Ended May 31, 2006
Net sales	$ 26.8	$ 50.1
Income (loss) from discontinued operations, net of taxes	$ .2	$ (1.7)

Note F Income (Loss) Per Share

The following table sets forth a reconciliation of the numerator and denominator used in the basic and diluted income (loss) per share and the computation of basic and diluted income (loss) per share:

	Three Months Ended May 31,		Six Months Ended May 31,	
	2007	**2006**	**2007**	**2006**
Numerator				
Income (loss) from continuing operations	**$ (9.8)**	$ 5.1	**$ (14.9)**	$ 2.7
Income (loss) from discontinued operations, net of tax		.2		(1.7)
Net income (loss)	**$ (9.8)**	$ 5.3	**$ (14.9)**	$ 1.0
		(Shares in millions)		
Denominator				
Denominator for basic earnings per share weighted average shares outstanding	**41.8**	41.3	**41.7**	41.2
Effect of dilutive securities		.4		.3
Denominator for dilutive earnings per share adjusted weighted average shares and assumed conversions	**41.8**	41.7	**41.7**	41.5
Basic and Diluted Income (Loss) Per Share				
Income (loss) from continuing operations	**$ (.23)**	$ .13	**$ (.36)**	$ .06
Income (loss) from discontinued operations				(.04)
Net income (loss)	**$ (.23)**	$ .13	**$ (.36)**	$ .02

Options to purchase common stock and unearned restricted stock of the Company totaling 4.2 million shares and 3.9 million shares during the second quarters of 2007 and 2006, respectively, and 4.2 million and 4.0 million during the first half of 2007 and 2006, respectively, were not included in the computation of dilutive per share amounts as they would have had an anti-dilutive effect.

Note G Share-Based Employee Compensation

The OMNOVA Solutions Second Amended and Restated 1999 Equity and Performance Incentive Plan (the Plan) permits the Company to grant to officers, key employees and non-employee directors of the Company, incentives directly linked to the price of OMNOVA Solutions common stock. The Plan authorizes up to an aggregate of 6.6 million shares of Company stock for awards of options to purchase shares of OMNOVA Solutions common stock, performance stock and performance units, restricted stock, deferred stock or appreciation rights. Shares used may be either newly issued shares or treasury shares or both. All options granted under the Plan have been granted at exercise prices equal to the market value of the Company s common stock on the date of grant. Additionally, the Plan provides that the term of any stock option granted under the Plan may not exceed 10 years. The second amendment to the Plan, which was approved by shareholders on March 22, 2007, also added a fungible share design, changed share counting provisions and dividend rights, added additional metrics to management objectives and other administrative changes. As of May 31, 2007, approximately 2.7 million shares of Company common stock remained available for grants under the Plan.

Stock options granted under the GenCorp 1993 and 1997 Stock Option Plans (GenCorp Options) to OMNOVA Solutions employees and GenCorp employees prior to the spin-off were partially converted into OMNOVA Solutions options and partially into GenCorp options with adjustments to preserve their value. The OMNOVA Solutions options, which were issued pursuant to the conversion process, were granted under the OMNOVA Solutions Inc. Option Adjustment Plan (the Adjustment Plan). The Adjustment Plan authorized up to 4.0 million shares of Company common stock solely for the purpose of accomplishing the conversion described above. Shares used may be either newly issued shares or treasury shares or both. No further options may be granted under the Adjustment Plan.

The fair value of each option award is estimated, with the assistance of an outside consulting service using a Black-Scholes based option valuation model. The risk-free rate is based on the U.S. Treasury yield curve in effect at the time of grant for periods within the contractual life of the option. The expected volatility is based on a blend of the Company s peer group in the industry in which it does business and the Company s historical volatility. The expected term of options granted is estimated considering the vesting periods and historical trends within the Company s equity plans and represents the period of time that options granted are expected to be outstanding. Estimates of fair value are not intended to predict actual future events or the value ultimately realized by employees who receive equity awards, and subsequent events are not indicative of the reasonableness of the original estimates of fair value made by the Company under SFAS No. 123 (Revised).

There were 1,000 stock options granted with a weighted average grant date fair value of $3.05, 12,687 stock options exercised and 594,179 stock options expired or forfeited during the first half of 2007. The weighted average grant date fair values of options granted during the first half of 2006 was $2.73.

Restricted stock grants consist of the Company s common stock. The Board set a two or three year vesting period for most of the issued restricted shares. The fair value of each restricted share grant is equal to the market price of the Company s common stock at the date of grant. Expense relating to restricted shares is amortized ratably over the vesting period.

During the first half of 2007, there were 19,712 restricted and deferred stock grants awarded, 38,200 restricted shares vested and 875 restricted shares forfeited.

Compensation expense for all share-based payments, included in general and administrative expense, was $0.2 million during each of the second quarters of 2007 and 2006 and $0.4 million during the first half of both 2007 and 2006.

As of May 31, 2007, there was $1.2 million of total unrecognized compensation cost related to non-vested share-based compensation arrangements.

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Note H Comprehensive Income (Loss)

The components of comprehensive income (loss) were as follows:

	Three Months Ended May 31,		Six Months Ended May 31,	
	2007	**2006**	**2007**	**2006**
Net income (loss)	**$ (9.8)**	$ 5.3	**$ (14.9)**	$ 1.0
Employee benefit plan amendment	**4.9**		**4.9**	
Foreign currency translation adjustment, net of tax	**.8**	2.4	**1.4**	3.3
Comprehensive income (loss)	**$ (4.1)**	$ 7.7	**$ (8.6)**	$ 4.3

Note I Employee Benefit Plans

The following table sets forth a reconciliation of the components of net periodic benefit costs for the Company s retirement programs:

	Pension Plans		Health Care Plans	
Three months ended May 31, 2007 and 2006	**2007**	**2006**	**2007**	**2006**
Service costs	**$ .9**	$ 1.2	**$ .1**	$ .1
Interest costs	**3.1**	2.8	**.3**	.3
Expected return on assets	**(3.8)**	(3.8)		
Amortization of net loss (gain)	**.9**	.9		(.1)
Amortization of prior service costs	**.2**	.3	**(.6)**	(.6)
Net periodic cost	**$ 1.3**	$ 1.4	**$ (.2)**	$ (.3)

	Pension Plans		Health Care Plans	
Six months ended May 31, 2007 and 2006	**2007**	**2006**	**2007**	**2006**
Service costs	**$ 1.9**	$ 2.3	**$ .1**	$ .2
Interest costs	**6.2**	5.7	**.6**	.6
Expected return on assets	**(7.6)**	(7.6)		
Amortization of net loss (gain)	**1.8**	1.8		(.1)
Amortization of prior service costs	**.4**	.6	**(1.2)**	(1.2)
Net periodic cost	**$ 2.7**	$ 2.8	**$ (.5)**	$ (.5)

In April 2007, the Company amended its retiree medical healthcare plan limiting salaried employee participation to those salaried employees who are eligible to retire as of March 31, 2007 and who retire by December 31, 2007. As a result, the Company expects to record additional income of $0.4 million for this plan in the second half of 2007 and $0.8 million in 2008.

Based on current pension asset performance, interest rate and discount rate assumptions, the Company does not anticipate making cash contributions to the pension fund before 2010.

The Company also sponsors a defined contribution pension plan. Participation in this plan is available to substantially all U.S. based employees. Contributions to this plan are based on either a percentage of employee contributions or on the provisions of the applicable collective bargaining agreement. The cost of this plan was approximately $0.6 million and $0.4 million for the three months ended May 31, 2007 and 2006, respectively, and approximately $1.2 million and $0.9 million for the first half of 2007 and 2006, respectively.

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Note I Employee Benefit Plans (Continued)

The Company also contributes to a defined contribution plan for its U.K. employees. The Company contributes a percentage of the employees wages depending upon the age of the employee. The cost of this plan was approximately $0.2 million and $0.1 million for the three month periods ended May 31, 2007 and 2006 and $0.4 million and $0.3 million for the first half of 2007 and 2006.

Note J Restructuring and Severance

In the second quarter and first half of 2007, the Company recognized $0.1 million and $0.4 million, respectively, of additional severance expense related to restructuring actions initiated during the fourth quarter of 2006.

The following table summarizes the Company s liabilities related to restructuring and severance activities:

	November 30, 2006	2007 Provision	Payments	May 31, 2007
Performance Chemicals	$ .4	$	$ .3	$ .1
Decorative Products	.5	.2	.6	.1
Corporate	.1	.2	.2	.1
Total	$ 1.0	$ .4	$ 1.1	$ .3

Note K Contingencies

From time to time, the Company is subject to various claims, lawsuits and proceedings related to product liability, product warranty, contract, employment, environmental and other matters arising out of the Company s business. The ultimate resolution of any litigation is inherently unpredictable. As a result, the Company s estimates of liability, if any, are subject to change and actual results may materially differ from the Company s estimates. Based on information that is currently available, the Company does not expect that the ultimate resolution of pending claims, lawsuits and proceedings will materially affect the consolidated financial condition of the Company. The effect that the ultimate resolution of these matters may have on results of operations cannot be predicted because any such effect depends on both future results of operations and the amount and timing of the resolution of these matters.

Note L Business Segment Information

Segment information has been prepared in accordance with SFAS No. 131, Disclosures About Segments of an Enterprise and Related Information. The Company s two operating segments were determined based on products and services provided. Accounting policies of the segments are described in Note A Basis of Presentation in both this Quarterly Report on Form 10-Q and the Company s Annual Report on Form 10-K.

The Company s two operating business segments are: Performance Chemicals and Decorative Products. The Company s operating segments are strategic business units that offer different products and services. They are managed separately based on fundamental differences in their operations.

The Performance Chemicals segment produces a broad range of emulsion polymers and specialty chemicals based primarily on styrene butadiene, styrene butadiene acrylonitrile, polyvinyl acetate, acrylic, styrene acrylic, vinyl acrylic, glyoxal, and fluorochemical chemistries. The segment s custom-formulated products include coatings, binders and adhesives, which are used in paper, carpet, nonwovens, textiles, construction, floor polish, masking tape, adhesives, tire cord, plastic parts and various other applications. Its products provide a variety of functional properties to enhance the Company s customers products, including greater strength, adhesion, dimensional stability, water resistance, flow and leveling, improved processibility and enhanced appearance.

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Note L Business Segment Information (Continued)

The Performance Chemicals segment consists of two product lines. The Paper and Carpet Chemicals product line encompasses products that have applications in the paper and carpet industries. Paper coatings are used in magazines, catalogs, direct mail advertising, brochures, printed reports, food cartons, household and other consumer and industrial packaging. Carpet binders are used to secure carpet fibers to carpet backing and meet the stringent manufacturing, environmental, odor, flammability and flexible installation requirements. The Specialty Chemicals product line encompasses products that have applications for nonwovens (such as diapers, engine filters, resilient flooring underlay, roofing mat, shoe components and household scrub pads), construction, adhesives, masking tape, tire cord, floor polish, textiles, graphic arts and plastic part coatings.

The Decorative Products segment develops, designs, produces and markets a broad line of decorative and functional surfacing products, including commercial wallcoverings, coated and performance fabrics, printed and solid color surface laminates and industrial films. These products are used in numerous applications, including commercial building refurbishment, remodeling and new construction, residential cabinets, flooring and furnishings, transportation markets including school busses, marine and automotive, performance films and fabric and manufactured housing.

The Decorative Products segment consists of three product lines. The Contract Interiors (formerly Commercial Wallcoverings) product line applications include refurbishment and new construction for the commercial office, hospitality, health care, retail, education, restaurant markets, residential furniture, commercial furniture and interior construction. The Coated Fabrics product line applications include marine and transportation seating, performance films and soft top covers. The Laminates product line applications include manufactured housing, recreational vehicle interiors, kitchen and bath cabinets, residential furniture, office furniture, consumer electronics and retail display.

Effective December 1, 2006, the Company renamed its Commercial Wallcoverings product line Contract Interiors and realigned certain products from the Coated Fabrics product line to Contract Interiors in order to better reflect common sales and marketing resources used to serve customers. All prior period amounts have been reclassified to conform to current year presentation.

The Company s operations are located primarily in the United States and Europe. No one customer accounted for 10% or more of consolidated sales.

Segment operating profit represents net sales less applicable costs, expenses and provisions for restructuring and severance costs, asset write-offs and work stoppage costs relating to operations. However, management excludes restructuring and severance costs, asset write-offs and work stoppage costs when evaluating the results of the segments.

Segment operating profit excludes unallocated corporate headquarters expenses, provisions for corporate headquarters restructuring and severance, interest expense and income taxes. Corporate headquarters expense includes the cost of providing and maintaining the corporate headquarters functions, including salaries, rent, travel and entertainment expenses, depreciation, utility costs, outside services and amortization of deferred financing costs.

The following table sets forth a summary of operations by segment and a reconciliation of segment sales to consolidated sales and segment operating profit to consolidated income (loss) from continuing operations before income taxes.

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Note L Business Segment Information (Continued)

	Three Months Ended May 31, 2007	Three Months Ended May 31, 2006	Six Months Ended May 31, 2007	Six Months Ended May 31, 2006
Net Sales				
Performance Chemicals				
Paper and Carpet Chemicals	**$ 75.3**	$ 72.9	**$ 145.8**	$ 145.0
Specialty Chemicals	**41.1**	38.5	**76.4**	75.8
Total Performance Chemicals	**$ 116.4**	$ 111.4	**$ 222.2**	$ 220.8
Decorative Products				
Contract Interiors	**$ 31.0**	$ 28.1	**$ 59.4**	$ 56.4
Coated Fabrics	**21.4**	18.5	**37.2**	34.3
Laminates	**19.2**	19.8	**34.0**	36.1
Total Decorative Products	**$ 71.6**	$ 66.4	**$ 130.6**	$ 126.8
Total Net Sales	**$ 188.0**	$ 177.8	**$ 352.8**	$ 347.6
Segment Operating Profit				
Performance Chemicals	**$ 5.8**	$ 8.9	**$ 9.4**	$ 14.1
Decorative Products	**4.2**	4.7	**3.4**	5.9
Total Segment Operating Profit	**$ 10.0**	$ 13.6	**$ 12.8**	$ 20.0
Interest expense	**(4.6)**	(5.2)	**(9.3)**	(10.4)
Corporate expense	**(2.8)**	(3.2)	**(6.0)**	(6.8)
Debt redemption expense	**(12.4)**		**(12.4)**	
Income (Loss) From Continuing Operations Before Income Taxes	**$ (9.8)**	$ 5.2	**$ (14.9)**	$ 2.8

The following table sets forth certain financial information relating to the Company s unconsolidated Asian joint ventures:

	Three Months Ended May 31, 2007	Three Months Ended May 31, 2006	Six Months Ended May 31, 2007	Six Months Ended May 31, 2006
CPPC - Decorative Products Co., Ltd.				
Net sales	**$ 13.6**	$ 9.6	**$ 22.7**	$ 18.9
Gross profit	**$ .9**	$ .6	**$ 1.1**	$ .8
Operating income	**$ .4**	$ .3	**$ .5**	$ .1
Net income	**$ .4**	$ .3	**$ .5**	$ .1
CG - OMNOVA Decorative Products (Shanghai) Co., Ltd.				
Net sales	**$ 13.7**	$ 13.7	**$ 26.6**	$ 24.1
Gross profit	**$ 1.7**	$ 3.0	**$ 2.7**	$ 4.8
Operating income	**$ .9**	$ 2.3	**$ .9**	$ 3.3
Net income	**$ .9**	$ 2.1	**$ .9**	$ 2.9

Note M Income Taxes

The Company did not record an income tax expense or benefit during the second quarters of 2007 or 2006.

As of November 30, 2006, the Company had approximately $114.2 million of domestic federal net operating loss carryforwards (NOL s) and $204.0 million of state and local NOL s with carryforward periods of 20 years and 5 to 20 years, respectively. The majority of the federal and state and local NOL s expire in the years 2020 through 2025. Due to the Company s history of cumulative losses, the Company has provided a full valuation allowance of approximately $91.8 million against its net deferred tax assets due to the uncertainty of realization of such assets.

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

The Company is an innovator of emulsion polymers and specialty chemicals and decorative and functional surfaces for a variety of commercial, industrial and residential end uses. The Company operates in two reportable business segments: Performance Chemicals and Decorative Products. The Performance Chemicals segment produces a broad range of emulsion polymers and specialty chemicals based primarily on styrene butadiene, styrene butadiene acrylonitrile, vinyl pyridine, polyvinyl acetate, acrylic, styrene acrylic, vinyl acrylic, glyoxal and fluorochemical chemistries. Performance Chemicals custom-formulated products include coatings, binders and adhesives, which are used in paper, carpet, nonwovens, textiles, construction, floor polish, masking tape, adhesives, tire cord, plastic parts and various other applications. The Decorative Products segment develops, designs, produces and markets a broad line of decorative and functional surfacing products, including commercial wallcoverings, coated and performance fabrics, printed and solid color surface laminates and industrial films. These products are used in numerous applications, including commercial building refurbishment, remodeling and new construction, residential cabinets, flooring and furnishings, transportation markets including school busses, marine and automotive, performance films and fabric and manufactured housing.

The Company s products are sold to manufacturers, independent distributors and end-users through internal marketing and sales forces and agents.

The Company has strategically located manufacturing facilities in the U.S. and U.K. along with its joint venture manufacturing facilities in China and Thailand.

The Company has historically experienced stronger sales and income in its second, third and fourth quarters, comprised of the three-month periods ending May 31, August 31 and November 30. The Company s performance in the first quarter (December through February) has historically been weaker due to generally lower levels of customer manufacturing, refurbishment and construction over the holidays and cold weather months.

The Company s chief operating decision maker evaluates performance and allocates resources by operating segment. Segment information has been prepared in accordance with the Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards (SFAS) No. 131 Disclosures About Segments of an Enterprise and Related Information. The Company s two operating segments were determined based on products and services provided. Accounting policies of the segments are described in Note A Basis of Presentation in both this Quarterly Report on Form 10-Q and the Company s Annual Report on Form 10-K. For a reconciliation of the Company s segment operating performance information to consolidated operating performance information, please refer to Note L of the Company s Unaudited Interim Consolidated Financial Statements.

Effective December 1, 2006, the Company renamed its Commercial Wallcoverings product line Contract Interiors and realigned certain product sales from the Coated Fabrics product line to Contract Interiors in order to better reflect common sales and marketing resources used to serve customers. All prior period amounts have been reclassified to conform to current year presentation.

Key Indicators

Key economic measures relevant to the Company include coated paper production, print advertising spending, U.S. commercial real estate and hotel occupancy rates, U.S. office furniture sales, manufactured housing shipments, housing starts and sales of existing homes and forecasts of raw material pricing for certain petrochemical feed stocks. Key OEM industries which provide a general indication of demand drivers to the Company include paper, commercial building construction, housing, furniture manufacturing and flooring manufacturing. These measures provide general information on trends relevant to the demand for the Company s products but the trend information does not necessarily directly correlate with demand levels in the markets which ultimately use the Company s products.

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Key operating measures utilized by the business segments include orders, sales, working capital turnover, inventory, productivity, new product vitality and order fill-rates which provide key indicators of business trends. These measures are reported on various cycles including daily, weekly and monthly depending on the needs established by operating management.

Key financial measures utilized by the Company s management and business segments in order to evaluate the results of its business and in understanding key variables impacting the current and future results of the Company include: sales, gross profit, selling, general and administrative expenses, operating profit before excluded items, adjusted earnings before interest, taxes, depreciation and amortization as set forth in the Company s senior secured revolving credit facility (Adjusted EBITDA), working capital, operating cash flows, capital expenditures and earnings per share before excluded items, including applicable ratios such as inventory turnover, average working capital and return on sales and assets. These measures, as well as objectives established by the Board of Directors of the Company, are reviewed at monthly, quarterly and annual intervals and compared with historical periods.

Results of Operations for the Three and Six Months Ended May 31, 2007 and 2006

The Company s net sales for the three months ended May 31, 2007 were $188.0 million compared to $177.8 million for the three months ended May 31, 2006. The Decorative Products segment experienced a revenue increase of $5.2 million or 7.8%, while the Performance Chemicals segment experienced an increase of $5.0 million or 4.5%. Contributing to the sales increase in the second quarter of 2007 were improved unit volumes of $4.6 million, sales price increases of $3.6 million and favorable foreign exchange translation of $2.0 million. Gross profit decreased to $37.1 million, with gross profit margin of 19.7%, in the second quarter of 2007 as compared to $40.9 million, with a gross profit margin of 23.0%, in the second quarter of 2006. Gross profit declined because cost of goods sold for the second quarter of 2007 increased $14.0 million to $150.9 million versus the same quarter last year driven by higher raw material costs of $6.5 million, increased transportation costs of $0.9 million, higher volume of $1.5 million and manufacturing costs of $5.1 million.

Net sales for the six months ended May 31, 2007 were $352.8 million compared to $347.6 million for the six months ended May 31, 2006. Gross profit for the six months ended May 31, 2007 declined to $67.2 million, with gross profit margin of 19.0%, compared to $75.0 million, with gross profit margin of 21.6%, for the six months ended May 31, 2006.

The Company had segment operating profit of $10.0 million in the second quarter of 2007 compared to segment operating profit of $13.6 million in the same period in 2006. Operating margins in the second quarter of 2007 were 5.3% compared to 7.6% in the same period of 2006. The decrease in segment operating profit was primarily due to higher raw materials, transportation and manufacturing costs, partially offset by pricing actions and cost reductions.

The Company had segment operating profit of $12.8 million in the first half of 2007 compared to segment operating profit of $20.0 million in the first half of 2006. The decrease in segment operating profit was primarily due to lower volume, higher raw materials, transportation, manufacturing and healthcare costs, partially offset by pricing actions and cost reductions. Segment operating profit also includes items which management excludes when evaluating the results of the Company s segments. Those items for the first half of 2007 included restructuring and severance charges of $0.2 million resulting primarily from previously announced workforce reductions.

The net loss was $9.8 million in the second quarter of 2007, or a loss of $0.23 per diluted share, compared to net income of $5.3 million, or $0.13 per diluted share in the second quarter of 2006. The Company had a net loss of $14.9 million in the first half of 2007, or $0.36 per diluted share, compared to net income of $1.0 million, or $0.02 per diluted share in the first half of 2006. Included in the second quarter and first half of 2007 are debt redemption costs of $12.4 million and restructuring and severance costs of $0.1 million.

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Performance Chemicals

Performance Chemicals net sales increased 4.5% to $116.4 million during the second quarter of 2007 compared to $111.4 million during the second quarter of 2006, driven by product pricing actions of $3.3 million, higher volume of $1.2 million and $0.5 million of favorable foreign exchange rates. Net sales for the Paper and Carpet chemicals product line increased to $75.3 million during the second quarter of 2007 compared to $72.9 million during the second quarter of 2006 as a result of pricing actions of $2.8 million, partially offset by lower volume of $0.4 million as a result of the slow down in the carpet industry resulting from lower new housing starts. Net sales for the Specialty Chemicals product line increased to $41.1 million during the second quarter of 2007 compared to $38.5 million during the second quarter of 2006, primarily due to higher volume of $1.6 million and pricing actions of $0.5 million.

This segment generated an operating profit of $5.8 million for the second quarter of 2007 compared to $8.9 million in the second quarter of 2006. The decrease in segment operating profit was due to higher raw material costs of $7.1 million and transportation costs of $0.8 million, partially offset by pricing actions of $3.3 million and higher volumes and cost reductions of $1.5 million.

Performance Chemicals net sales increased to $222.2 million during the first half of 2007 compared to $220.8 million during the first half of 2006, driven by product pricing actions of $5.4 million and $1.0 million of favorable foreign exchange rates, partially offset by lower volume of $5.0 million. Net sales for the Paper and Carpet chemicals product line increased 0.6% to $145.8 million during the first half of 2007 compared to $145.0 million during the first half of 2006 primarily as a result of pricing actions of $4.5 million, partially offset by lower volumes as a result of the slow down in the carpet industry resulting from lower new housing starts. Net sales for the Specialty Chemicals product line increased 0.8% to $76.4 million during the first half of 2007 compared to $75.8 million during the first half of 2006, primarily due to pricing actions and favorable foreign exchange translation of $1.9 million partially offset by lower volume.

This segment generated an operating profit of $9.4 million for the first half of 2007 compared to $14.1 million in the first half of 2006. The decrease in segment operating profit was due to lower sales volume of $2.1 million, higher raw material costs of $10.1 million, transportation costs of $1.5 million and healthcare costs of $0.2 million, partially offset by pricing actions of $5.4 million and cost reductions of $3.8 million.

Decorative Products

Decorative Products net sales increased by 7.8% to $71.6 million in the second quarter of 2007 from $66.4 million in the second quarter of 2006. Contract Interiors net sales of $31.0 million during the second quarter of 2007 were 10.3%, or $2.9 million, higher than the second quarter of 2006, primarily as a result of higher volume in the domestic wallcovering market and favorable foreign exchange rates from the British Pound Sterling and the Euro. Net sales for the Coated Fabrics product line increased 15.7% to $21.4 million during the second quarter of 2007 compared to $18.5 million during the second quarter of 2006, primarily as a result of higher volume in transportation. Net sales for the Laminates product line decreased 3.0% to $19.2 million during the second quarter of 2007 compared to $19.8 million during the second quarter of 2006 primarily due to lower volume in kitchen and bath.

This segment generated an operating profit of $ 4.2 million during the second quarter of 2007 compared to $4.7 million during the second quarter of 2006. The decrease in operating profit for the second quarter of 2007 as compared to the second quarter of 2006 was due to higher manufacturing and maintenance costs of $0.3 million, labor contract negotiation costs of $0.2 million, ERP system implementation costs of $0.3 million and lower income from the Company s joint ventures of $0.6 million due to higher raw material costs, partially offset by pricing actions of $0.3 million and lower raw material costs of $0.6 million.

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Decorative Products net sales increased by 3.0% to $130.6 million in the first half of 2007 from $126.8 million in the first half of 2006. Contract Interiors net sales of $59.4 million during the first half of 2007 were $3.0 million higher than the first half of 2006 primarily due to favorable foreign exchange translation from the British Pound Sterling and the Euro. Net sales for the Coated Fabrics product line increased 8.5% to $37.2 million during the first half of 2007 compared to $34.3 million during the first half of 2006, primarily as a result of higher volume in transportation and industrial films, partially offset by lower volumes in rigid films. Net sales for the Laminates product line decreased 5.8% to $34.0 million during the first half of 2007 compared to $36.1 million during the first half of 2006 primarily due to lower volumes in kitchen and bath, manufactured housing and flooring, partially offset by higher volume in furniture and display.

This segment generated an operating profit of $3.4 million during the first half of 2007 compared to $5.9 million during the first half of 2006. The lower operating profit for the first half of 2007, as compared to the first half of 2006 was due to lower volume of $1.0 million, higher manufacturing and maintenance costs of $1.3 million, higher quality control costs of $0.3 million, ERP system implementation costs of $0.7 million and lower income from the Company s joint ventures of $0.8 million due to higher raw material costs in Asia, partially offset by lower domestic raw material costs of $1.3 million and pricing actions of $0.5 million. The segment s operating profit also includes items which management excludes when evaluating the results of the Company s segments. Those items for the first half of 2007 were restructuring and severance charges of $0.2 million resulting primarily from workforce reductions previously announced in the fourth quarter of 2006.

Corporate

Interest expense for the second quarter and first six months of 2007 was $4.6 million and $9.3 million, respectively, compared to $5.2 million and $10.4 million for the second quarter and first six months of 2006, respectively. The decrease is primarily due to lower average debt outstanding.

As described under Long Term Debt, on May 22, 2007, the Company entered into a $150 million Term Loan Credit Agreement (Term Loan). The Term Loan carries a variable interest rate based on, at the Company s option, either an alternate base rate or a eurodollar rate, in each case plus an applicable margin. The proceeds of the Term Loan, along with cash and other resources of the Company, were used to redeem $162 million of its $165 million 11 1/4% Senior Secured Notes. The remaining $3 million were redeemed on June 22, 2007. As a result of the tender offer the Company paid $9.8 million in premium and tender fees and wrote off $2.6 million of unamortized bond issuance costs. Additionally, the Company entered into a $50 million notional amount interest rate swap to fix the interest rate on a portion of the Term Loan. As of May 31, 2007, the weighted average interest rate on the Company s outstanding debt was 7.77%, a reduction of 348 basis points, compared to the redeemed Senior Secured Notes. At debt levels and weighted average interest rates which existed at May 31, 2007, the Company s annualized interest expense savings would be approximately $6.0 million. As a portion of the interest rates are variable, future interest rates may increase or decrease and the Company s future debt levels may change due to required or voluntary principle payments. Therefore, actual interest expense savings may be materially different.

Corporate expenses were $2.8 million and $6.0 million during the second quarter and first six months of 2007, respectively, compared to $3.2 million and $6.8 million during the second quarter and first six months of 2006, respectively. For the quarter and first six months, the decrease was primarily due to lower incentive and deferred compensation plan expense compared to the prior year.

The Company did not record a tax expense during the first six months of 2007 compared to tax expense of $0.1 million, relating to foreign income taxes, during the first six months of 2006. The Company s estimated effective income tax rate of 0% is substantially less than its federal statutory rate of 35% primarily due to the current period net loss being fully offset by a valuation allowance. Due to the Company s history of cumulative losses, the Company has provided a full valuation allowance of approximately $91.8 million against its net deferred tax assets due to the uncertainty of realization of such assets. As discussed in Footnote M - Income Taxes, as of November 30, 2006, the Company had approximately $114.2 million of domestic federal net operating losses with a carryforward period of approximately 20 years.

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Discontinued Operations

On September 27, 2006, the Company sold substantially all of the assets and liabilities of the Building Products business to BFS Diversified Products, LLC, for $25.9 million in cash resulting in a gain of $18.2 million. No income taxes were provided due to the utilization of a portion of the Company s net operating loss carryforwards. The Company retained $10.5 million of Building Products trade accounts receivable, all of which were collected as of November 30, 2006.

In accordance with the provisions of SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, the results of operations and cash flows of the Building Products business for all periods presented have been reported as discontinued operations. This transaction allows the Company to focus its resources on its strategic product lines with strong market positions and will provide the Company with flexibility to grow its remaining segments.

(Dollars in millions)	Three Months Ended May 31, 2006	Six Months Ended May 31, 2006
Net sales	$ 26.8	$ 50.1
Income (loss) from discontinued operations, net of taxes	$ .2	$ (1.7)

Restructuring and Severance

In the second quarter and first half of 2007, the Company recognized $0.1 million and $0.4 million, respectively, of additional severance expense related to restructuring actions initiated during the fourth quarter of 2006.

Financial Resources and Capital Spending

The following table reflects key cash flow measures from continuing operations:

	Six Months Ended May 31,		
(Dollars in millions)	2007	2006	Change
Cash used in operating activities	$ (10.6)	$ (2.6)	$ (8.0)
Cash provided by (used) in investing activities	$ 6.2	$ (4.2)	$ 10.4
Cash (used) in provided by financing activities	$ (9.8)	$ 9.3	$ (19.1)
(Decrease) increase in cash and cash equivalents	$ (12.8)	$ 5.3	$ 18.1

Cash used by operating activities was $10.6 million in the first half of 2007, compared to $2.6 million in the first half of 2006. Cash used by operations increased in 2007 primarily due to an increase in working capital and operating loss.

In the first half of 2007, $6.2 million was provided by investing activities, as compared to $4.2 million used for investing activities in the first half of 2006. During 2007, the Company redeemed $12.5 million of restricted cash in connection with its debt redemption and refinancing, as described in Note D Long-Term Debt. Additionally, the Company incurred $6.1 million of capital expenditures in the first half of 2007, compared to $3.7 million in the first half of 2006. Capital expenditures were made and are planned principally for asset replacement, new product capability, cost reduction, safety and productivity improvements and environmental protection. The Company anticipates capital expenditures in 2007 to be approximately $18.0 million. The Company plans to fund substantially all of its capital expenditures from anticipated cash flow generated from operations during the remainder of the year. If necessary, a portion of capital expenditures will be funded through borrowings under its current credit facility.

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Cash used for financing activities in the first half of 2007 was $9.8 million compared to cash provided of $9.3 million in the first half of 2006. The first half of 2007 includes costs associated with the Company s debt refinancing including $12.0 million for debt redemption expense, a $2.6 million write-off of deferred financing costs and $3.4 million which has been reserved for the redemption of the remaining Senior Secured Notes in June 2007. Cash provided by financing activities in the first half of 2006 was primarily related to borrowings under the revolving credit facility. Total debt was $173.0 million as of May 31, 2007, compared to $165.0 million as of November 30, 2006 and $185.0 million as of May 31, 2006.

Long-Term Debt

On May 22, 2007, the Company entered into a $150 million Term Loan Credit Agreement (Term Loan) due May 2014. The Term Loan carries a variable interest rate based on, at the Company s option, either an alternate base rate or a eurodollar rate, in each case plus an applicable margin. The alternate base interest rate is a fluctuating rate equal to the higher of the Prime Rate or the sum of the Federal Funds Effective Rate plus 50 basis points. The applicable margin for the alternate base rate is 150 basis points. The eurodollar rate is a periodic fixed rate equal to the London Inter Bank Offered Rate (LIBOR). The applicable margin for the eurodollar rate is 250 basis points. Annual principal payments consists of $1.5 million, which are due in quarterly installments, and annual excess free cash flow payments as defined in the Term Loan agreement, with any remaining balance to be paid May 2014. The Company can prepay any amount at any time without penalty upon proper notice and subject to a minimum dollar requirement. The Term Loan is secured by all real property and equipment of the Company s domestic facilities and stock and equity investments of the Company s non-domestic subsidiaries. The Term Loan contains affirmative and negative covenants, including limitations on additional debt, certain investments and acquisitions outside of the Company s line of business. The Term Loan requires the Company to maintain a net leverage ratio of less than 5.5 to 1 and at May 31, 2007, the Company was in compliance with this requirement. The Term Loan also provides for additional borrowings of up to $75 million, provided that certain requirements are met including an interest coverage ratio and a senior secured leverage ratio.

Proceeds of the Term Loan, along with cash, restricted cash and other resources of the Company, were used to redeem $162 million of the Company s $165 million 11/4% Senior Secured Notes (Notes). In connection with the redemption of the Notes, the Company paid $9.8 million in premium and tender fees. Additionally, the Company wrote off $2.6 million of unamortized debt issuance costs which were being amortized over the term of the Notes. The remaining $3.0 million of Notes have been called, and were redeemed on June 22, 2007. As of May 31, 2007, the Company placed an amount equal to the principal, premium and accrued interest in a restricted cash account to redeem the remaining Notes.

On May 31, 2007, the Company entered into a fixed rate interest rate swap agreement totaling $50 million to convert a portion of the outstanding term loan from variable to fixed rates. Under this agreement, the Company will pay a fixed rate of 7.73% and receive a variable rate based on LIBOR plus a margin of 250 basis points. The variable rate is reset every three months, at which time the interest will be settled and will be recognized as adjustments to interest expense. This swap agreement is designated as a cash flow hedge, and as such, any resulting gain or loss on the derivative instrument will be recognized in accumulated other comprehensive income, until it is realized with a corresponding adjustment to long-term debt. The fair value of the swap as of May 31, 2007 was $0.

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In connection with the Term Loan, on May 22, 2007 the Company amended its senior secured revolving credit facility (Facility). The facility was increased to $80 million from $72 million and extended until May 2012. The Facility includes a $15 million sublimit for the issuance of commercial and standby letters of credit and a $10 million sublimit for swingline loans. Borrowings under the Facility are limited to a borrowing base using customary advance rates for eligible accounts receivable and inventory. Borrowings under the Facility are secured by domestic accounts receivable, inventory and intangible assets. The Facility contains affirmative and negative covenants, similar to the Term Loan, including limitations on additional debt, certain investments and acquisitions outside of the Company s line of business. If the average excess availability of the Facility falls below $20 million, the Company must maintain a fixed charge coverage ratio greater than 1.1 to 1 as defined in the agreement. The Company may request an increase in available borrowings under the Facility of up to $20 million (for a maximum of $100 million) upon satisfaction of certain requirements.

Advances under the Facility bear interest, at the Company s option, at either an alternate base rate or a eurodollar rate, in each case plus an applicable margin. The alternate base interest rate is a fluctuating rate equal to the higher of the Prime Rate or the sum of the Federal Funds Effective Rate plus 50 basis points. The applicable margin for the alternate base rate will vary from 0.0% to 0.25% depending on the Company s fixed charge coverage ratio and the margin was 0.0% at May 31, 2007. The eurodollar rate is a periodic fixed rate equal to LIBOR. The applicable margin for the eurodollar rate will vary from 1.25% to 2.0% depending on the Company s fixed charge coverage ratio and the margin was 1.5% at May 31, 2007.

The Facility requires a commitment fee based on the unused portion of the Facility. The commitment fee will vary from 0.125% to 0.25% based on the Company s fixed charge coverage ratio and was 0.125% at May 31, 2007.

At May 31, 2007, the available balance under the Facility, net of outstanding letters of credit and required reserves, was $56.6 million. Borrowings under the Facility were $20.0 million and standby letters of credit outstanding were $3.4 million as of May 31, 2007.

As of May 31, 2007, the weighted average interest rate on the Company s outstanding debt was 7.77%, a reduction of 348 basis points, compared to the redeemed Senior Secured Notes. At debt levels and weighted average interest rates, which existed at May 31, 2007, the Company s annualized interest expense savings would be approximately $6.0 million. As a portion of the interest rates are variable, future interest rates may increase or decrease and the Company s future debt levels may change due to required or voluntary principle payments, therefore, actual interest expense savings may be materially different.

Based upon current and anticipated levels of operations, the Company believes that its cash flows from operations, combined with borrowings that will be available under the Facility, will be sufficient to enable the Company to meet its current and anticipated cash operating requirements, including scheduled interest and principal payments, capital expenditures and working capital needs, for the next twelve months. Currently, the Company s long-term debt bears interest at variable rates; therefore, the Company s liquidity and financial condition will continue to be affected by changes in prevailing interest rates.

Employee Benefit Plans

In April 2007, the Company amended its retiree medical healthcare plan limiting salaried employee participation to those salaried employees who are eligible to retire as of March 31, 2007 and who retire by December 31, 2007. As a result, the Company expects to record additional income of $0.4 million for this plan in the second half of 2007 and $0.8 million in 2008.

Significant Accounting Policies and Management Judgments

The Company s discussion and analysis of its results of operations, financial condition and liquidity are based upon the Company s consolidated financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles. The preparation of these financial statements requires the Company to make estimates and judgments that affect the amounts of assets and liabilities, revenues and expenses and disclosure of contingent assets and liabilities as of the date of the financial statements. Periodically, the Company reviews its estimates and judgments including those related to product returns, accounts receivable, inventories, warranty obligations, litigation and environmental reserves, pensions and income taxes. The Company bases its estimates and judgments on historical experience and on various assumptions that it believes to be reasonable under the circumstances. Actual results may differ materially from these estimates and judgments under different assumptions.

Information with respect to the Company s significant accounting policies and management judgments which the Company believes could have the most significant effect on the Company s reported results and require subjective or complex judgments by management is contained in Management s Discussion and Analysis of Financial Condition and Results of Operations of the Company s Annual Report on Form 10-K for the year ended November 30, 2006, as filed with the SEC. The Company has not made any changes in estimates or judgments that have had a significant effect on the reported amounts.

Environmental Matters

The Company s policy is to conduct its businesses with due regard for the preservation and protection of the environment. The Company devotes significant resources and management attention to compliance with environmental laws and regulations. The Company s Consolidated Balance Sheet as of May 31, 2007 reflects an accrual for environmental remediation of $0.5 million. The Company s estimates are subject to change and actual results may materially differ from the Company s estimates. Management believes, on the basis of presently available information, that resolution of known environmental matters will not materially affect liquidity, capital resources or the consolidated financial condition of the Company. The effect that the ultimate resolution of these matters may have on results of operations cannot be predicted because any such effect depends on both future results of operations and the amount and timing of the resolution of such matters.

Employee Matters

The Company employs approximately 1,700 employees at offices, plants and other facilities located principally throughout the United States and the United Kingdom. The Company would generally describe its relationship with employees as good. Approximately 28% or about 480 of the Company s employees are covered by collective bargaining agreements. In February 2007, the Company and its Calhoun, Georgia bargaining unit employees ratified a new three year contract agreement. In May 2007, the Company and its Columbus, Mississippi bargaining unit employees ratified a new three year contract agreement.

New Accounting Pronouncements

In July 2006, the FASB issued Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109. FIN 48 clarifies the accounting for uncertainty in income taxes recognized by prescribing a recognition threshold and measurement attribute for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for years beginning after December 15, 2006. This interpretation will be effective for the Company beginning in the first quarter of 2008. The Company is in the process of determining the impact of this Interpretation on the Company s consolidated financial statements.

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In September 2006, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 157, Fair Value Measurements. SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. This Statement is effective for years beginning after November 15, 2007. The Company is in the process of determining the impact of this Statement on the Company s consolidated financial statements.

Effective November 30, 2006, the Company adopted the recognition provisions of SFAS No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R). This Statement requires employers to recognize in their balance sheets the overfunded or underfunded status of defined benefit post-retirement plans, measured as the difference between the fair value of plan assets and the benefit obligation (the projected benefit obligation for pension plans and the accumulated postretirement benefit obligation for other post-retirement plans). Employers must recognize the change in the funded status of the plan in the year in which the change occurs through other comprehensive income. This Statement also requires plan assets and obligations to be measured as of the employer s balance sheet date. The measurement provision of this Statement will be effective for years beginning after December 15, 2008, with early application encouraged. The Company has not yet adopted the measurement provisions of this Statement and is in the process of determining the impact of the adoption on the Company s consolidated financial statements.

Forward-Looking Statements

This quarterly report on Form 10-Q includes forward-looking statements, as defined by federal securities laws, with respect to the Company s financial condition, results of operations and business, among other things, and include statements based on the Company s current expectations, estimates, forecasts and projections. Words such as, but not limited to, may, should, projects, forecasts, seeks, believes, expects, antic estimates, intends, plans, targets, likely, will, would, could, and similar expressions or phrases identify forward-looking statements.

All forward-looking statements involve risks and uncertainties. Many risks and uncertainties are inherent in business generally and the markets in which the Company operates. Other risks and uncertainties are more specific to the Company s operations. These risks and uncertainties and the achievement of expected results depends on many factors, some or all of which are not predictable or within the Company s control. Actual results may differ materially from expected results.

Factors that may cause actual results to differ materially from expected results include, among others:

- General economic trends affecting the Company s end-use markets;
- Prices and availability of raw materials including styrene, butadiene, polyvinyl chloride, acrylics and textiles;
- Ability to increase pricing to offset raw material cost increases;
- Customer and/or competitor consolidation;
- Ability to successfully develop and commercialize new products;
- Customer ability to compete against increased foreign competition;
- Ability to successfully implement productivity enhancement and cost reduction initiatives;
- Operational issues at the Company s facilities;

The Company s strategic alliance and acquisition activities;

Acts of war or terrorism, natural disasters or other acts of God;

Governmental and regulatory policies;

Compliance with extensive environmental, health and safety laws and regulations;

Rapid inflation in health care costs and assumptions used in determining health care cost estimates;

Risks associated with foreign operations including fluctuations in exchange rates of foreign currencies;

Prolonged work stoppage resulting from labor disputes with unionized workforce;

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Assumptions used in determining pension plan expense and funding, such as return on assets and discount rates and changes in pension funding regulations;

Adverse litigation judgment and absence of or inadequacy of insurance coverage for such judgment;

Availability of financing to fund operations at anticipated rates and terms;

Substantial debt and leverage and the ability to service that debt;

Significant increase in applicable short-term borrowing rates; and

Other factors described in Item 1A of the Company s Annual Report on Form 10-K for the year ended November 30, 2006.

All written and verbal forward-looking statements attributable to the Company or any person acting on the Company s behalf are expressly qualified in their entirety by the risk factors and cautionary statements contained in Item 1A of the Company s Annual Report on Form 10-K for the year ended November 30, 2006 and herein. Any forward-looking statement speaks only as of the date on which such statement is made, and the Company undertakes no obligation, and specifically declines any obligation, other than that imposed by law, to publicly update or revise any forward-looking statements whether as a result of new information, future events or otherwise.

Item 3. Quantitative and Qualitative Disclosure About Market Risk

Quantitative and Qualitative Disclosure About Market Risk

The Company is exposed to market risk from changes in interest rates on its long-term debt obligations. As described in Note D to the Unaudited Interim Consolidated Financial Statements, the Company s $150 million Term Loan Credit Agreement, which matures in 2014 and senior secured revolving credit facility, which matures in 2012, are variable. Borrowings under the Term Loan and the Facility were $150 million and $20.0 million, respectively, as of May 31, 2007. The Company has one fixed rate interest rate swap agreement for $50 million, to convert a portion of its variable rate Term Loan to a fixed rate of 7.73%. The fair value of the swap was $0 as of May 31, 2007. The weighted average effective interest rate of the Company s outstanding debt was 7.77% as of May 31, 2007. A hypothetical increase or decrease of 100 basis points would impact the Company s interest expense by approximately $1.7 million. The Company does not enter into derivatives or other financial instruments for trading or speculative purposes.

The Company is subject to foreign currency exchange rate risk primarily due to the European wallcovering business. The Company has an accumulated gain of $6.3 million as of May 31, 2007, which is included in accumulated other comprehensive loss, primarily due to the favorable currency translation of the British Pound Sterling. To date, the Company has not entered into any significant foreign currency forward exchange contracts or other derivative financial instruments to hedge the effects of adverse fluctuations in foreign currency exchange rates, but will continue to evaluate the future use of these financial instruments.

Item 4. Controls and Procedures

Controls and Procedures

Management of the Company, including the Chief Executive Officer and the Chief Financial Officer, has evaluated the effectiveness of the Company s disclosure controls and procedures (as defined in Rules 13a 15(e) under the Securities Exchange Act of 1934) as of May 31, 2007, and, based on this evaluation, has determined that the Company s disclosure controls and procedures are effective as of such date. Further, during the quarter ended May 31, 2007, there were no changes in the Company s internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

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Part II. Other Information

Item 1. Legal Proceedings

From time to time, the Company is subject to various claims, lawsuits and proceedings related to product liability, product warranty, contract, employment, environmental and other matters arising out of the Company s business. The ultimate resolution of any litigation is inherently unpredictable. As a result, the Company s estimates of liability, if any, are subject to change and actual results may materially differ from the Company s estimates. Based on information that is currently available, the Company does not expect that the ultimate resolution of pending claims, lawsuits and proceedings will materially affect the consolidated financial condition of the Company. The effect that the ultimate resolution of these matters may have on results of operations cannot be predicted because any such effect depends on both future results of operations and the amount and timing of the resolution of these matters.

Item 1A. Risk Factors

There have been no material changes to the risk factors previously disclosed in Item 1A of the Company s Annual Report on Form 10-K for the year ended November 30, 2006. Those risk factors, in addition to the other information set forth in this report, could materially affect the Company s business, financial condition or results of operations. Additional unrecognized risks and uncertainties may materially adversely affect the Company s business, financial condition or results of operations.

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

At the Company s Annual Meeting of Shareholders held on March 22, 2007, holders of OMNOVA Solutions Common Stock elected David J. D Antoni, Diane E. McGarry and Steven W. Percy as directors to serve three-year terms expiring in 2010.

Shareholders also ratified the appointment of Ernst & Young LLP as the Company s independent registered public accounting firm for the 2007 fiscal year and approved the OMNOVA Solutions Inc. Second Amended and Restated 1999 Equity and Performance Incentive Plan.

Following are the final results of the votes cast:

a) Election of Directors:

	For	Withheld	Broker Non-votes
David J. D Antoni	37,223,987	663,286	-0-
Diane E. McGarry	37,220,888	666,385	-0-
Steven W. Percy	37,221,480	665,793	-0-

Ratification of the appointment of Ernst & Young LLP as Independent Registered Public Accounting Firm:

For: 37,739,974	**Against:** 102,283	**Abstain:** 45,016	**Broker Non-votes:** -0-

Approval of the OMNOVA Solutions Inc. Second Amended and Restated 1999 Equity and Performance Incentive Plan:

For: 26,797,844	**Against:** 5,883,957	**Abstain:** 168,865	**Broker Non-votes:** -0-

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Item 6. Exhibits

a) Exhibits

10.29	Amended and Restated Credit Agreement dated as of May 22, 2007 by and among OMNOVA Solutions Inc., as Borrower, the financial institutions party thereto, as Lenders, and JP Morgan Chase Bank N.A., as agent for the Lenders.
10.30	Term Loan Credit Agreement dated as of May 22, 2007 by and among OMNOVA Solutions Inc., as Borrower, the financial institutions party thereto, as Lenders, and Deutsche Bank Trust Company Americas, as Agent for the Lenders.
12.1	Computation of Ratio of Earnings to Fixed Charges.
31.1	Principal Executive Officer s Certifications pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Principal Financial Officer s Certifications pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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SIGNATURES

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

	OMNOVA Solutions Inc.
Date: June 29, 2007	By /s/ Michael E. Hicks Michael E. Hicks Senior Vice President and Chief Financial Officer; Treasurer (Principal Financial Officer and Principal Accounting Officer)
Date: June 29, 2007	By /s/ James C. LeMay James C. LeMay Senior Vice President, Business Development; General Counsel (Duly Authorized Officer)

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INDEX TO EXHIBITS

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