MCCORMICK & CO INC
Form 10-Q
June 27, 2014

UNITED STATES
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 Quarter Ended May 31, 2014
Commission File Number 001-14920

McCORMICK & COMPANY, INCORPORATED
(Exact name of registrant as specified in its charter)

MARYLAND	52-0408290
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
18 Loveton Circle, P. O. Box 6000, Sparks, MD	21152-6000
(Address of principal executive offices)	(Zip Code)
Registrant's telephone number, including area code	(410) 771-7301

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 filing requirements for the past 90 days. Yes ý No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "accelerated filer," "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer ý	Accelerated Filer ¨
Non-Accelerated Filer ¨	Smaller Reporting Company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No ý
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

	Shares Outstanding May 31, 2014
Common Stock	12,178,330
Common Stock Non-Voting	117,633,560

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

McCORMICK & COMPANY, INCORPORATED
CONDENSED CONSOLIDATED INCOME STATEMENT (UNAUDITED)
(in millions except per share amounts)

	Three months ended May 31,		Six months ended May 31,	
	2014	2013	2014	2013
Net sales	$1,033.4	$1,002.6	$2,026.8	$1,936.9
Cost of goods sold	620.9	608.2	1,222.8	1,180.8
Gross profit	412.5	394.4	804.0	756.1
Selling, general and administrative expense	290.8	278.4	557.7	528.1
Operating income	121.7	116.0	246.3	228.0
Interest expense	12.5	13.5	24.9	27.4
Other income, net	0.3	0.8	0.5	1.4
Income from consolidated operations before income taxes	109.5	103.3	221.9	202.0
Income taxes	31.2	30.6	66.2	58.8
Net income from consolidated operations	78.3	72.7	155.7	143.2
Income from unconsolidated operations	6.2	5.9	11.3	11.4
Net income	$84.5	$78.6	$167.0	$154.6
Earnings per share – basic	$0.65	$0.60	$1.28	$1.17
Average shares outstanding – basic	130.2	132.1	130.6	132.3
Earnings per share – diluted	$0.64	$0.59	$1.27	$1.16
Average shares outstanding – diluted	131.2	133.6	131.7	133.8
Cash dividends paid per share	$0.37	$0.34	$0.74	$0.68

See notes to condensed consolidated financial statements (unaudited).

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McCORMICK & COMPANY, INCORPORATED
CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (UNAUDITED)
(in millions)

	Three months ended May 31,		Six months ended May 31,	
	2014	2013	2014	2013
Net income	$84.5	$78.6	$167.0	$154.6
Net income attributable to non-controlling interest	0.7	0.4	1.7	0.9
Other comprehensive income (loss):				
Unrealized components of pension plans	4.1	9.2	7.9	22.1
Currency translation adjustments	(0.2)	(29.6)	4.1	(45.8)
Change in derivative financial instruments	(0.3)	3.5	—	7.7
Deferred taxes	(1.4)	(4.3)	(2.9)	(8.3)
Comprehensive income	$87.4	$57.8	$177.8	$131.2

See notes to condensed consolidated financial statements (unaudited).

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McCORMICK & COMPANY, INCORPORATED
CONDENSED CONSOLIDATED BALANCE SHEET
(in millions)

	May 31, 2014 (unaudited)	May 31, 2013 (unaudited)	November 30, 2013
ASSETS			
Current Assets			
Cash and cash equivalents	$81.4	$72.1	$63.0
Trade accounts receivables, net	417.1	399.9	495.5
Inventories			
Finished products	313.4	278.9	304.6
Raw materials and work-in-process	373.9	332.5	372.3
	687.3	611.4	676.9
Prepaid expenses and other current assets	138.9	134.1	134.8
Total current assets	1,324.7	1,217.5	1,370.2
Property, plant and equipment	1,448.0	1,364.0	1,407.7
Less: accumulated depreciation	(873.0)	(809.7)	(831.1)
Property, plant and equipment, net	575.0	554.3	576.6
Goodwill	1,798.6	1,754.2	1,798.5
Intangible assets, net	340.4	353.3	333.4
Investments and other assets	370.6	329.5	371.0
Total assets	$4,409.3	$4,208.8	$4,449.7
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current Liabilities			
Short-term borrowings	$307.1	$299.1	$211.6
Current portion of long-term debt	1.3	252.8	2.5
Trade accounts payable	335.8	322.1	387.3
Other accrued liabilities	358.6	352.2	461.7
Total current liabilities	1,002.8	1,226.2	1,063.1
Long-term debt	1,016.8	774.4	1,019.0
Other long-term liabilities	409.8	474.5	419.9
Total liabilities	2,429.4	2,475.1	2,502.0
Shareholders' Equity			
Common stock	363.5	346.9	352.8
Common stock non-voting	620.6	600.8	609.6
Retained earnings	969.3	953.2	970.4
Accumulated other comprehensive income (loss)	8.8	(184.2)	(0.3)
Non-controlling interests	17.7	17.0	15.2
Total shareholders' equity	1,979.9	1,733.7	1,947.7
Total liabilities and shareholders' equity	$4,409.3	$4,208.8	$4,449.7

See notes to condensed consolidated financial statements (unaudited).

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McCORMICK & COMPANY, INCORPORATED
CONDENSED CONSOLIDATED CASH FLOW STATEMENT (UNAUDITED)
(in millions)

	Six months ended May 31,	
	2014	2013
Cash flows from operating activities		
Net income	$167.0	$154.6
Adjustments to reconcile net income to net cash flow provided by operating activities:		
Depreciation and amortization	53.5	51.7
Stock-based compensation	12.1	12.5
Income from unconsolidated operations	(11.3)	(11.4)
Changes in operating assets and liabilities	(51.6)	(77.3)
Dividends from unconsolidated affiliates	12.4	2.6
Net cash flow provided by operating activities	182.1	132.7
Cash flows from investing activities		
Acquisition of business	—	(116.7)
Capital expenditures	(47.4)	(34.6)
Proceeds from sale of property, plant and equipment	0.7	1.9
Net cash flow used in investing activities	(46.7)	(149.4)
Cash flows from financing activities		
Short-term borrowings, net	94.3	158.9
Long-term debt repayments	(1.2)	(0.9)
Proceeds from exercised stock options	16.1	29.8
Common stock acquired by purchase	(126.3)	(92.1)
Dividends paid	(96.7)	(90.1)
Net cash flow (used in) provided by financing activities	(113.8)	5.6
Effect of exchange rate changes on cash and cash equivalents	(3.2)	4.2
Increase (decrease) in cash and cash equivalents	18.4	(6.9)
Cash and cash equivalents at beginning of period	63.0	79.0
Cash and cash equivalents at end of period	$81.4	$72.1

See notes to condensed consolidated financial statements (unaudited).

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McCORMICK & COMPANY, INCORPORATED
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. ACCOUNTING POLICIES

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and do not include all the information and notes required by United States generally accepted accounting principles (U.S. GAAP) for complete financial statements. In our opinion, the accompanying condensed consolidated financial statements contain all adjustments, which are of a normal and recurring nature, necessary to present fairly the financial position and the results of operations for the interim periods presented.

The results of consolidated operations for the three and six month periods ended May 31, 2014 are not necessarily indicative of the results to be expected for the full year. Historically, our net sales, net income and cash flow from operations are lower in the first half of the fiscal year and increase in the second half. The typical increase in net sales, net income and cash flow from operations in the second half of the year is largely due to the consumer business cycle in the U.S., where customers typically purchase more products in the fourth quarter due to the Thanksgiving and Christmas holiday seasons.

For further information, refer to the consolidated financial statements and notes included in our Annual Report on Form 10-K for the year ended November 30, 2013.

Reclassification

To conform to our current year presentation, inventories of $14.3 million have been reclassified from Finished products to Raw materials and work-in-process in our condensed consolidated balance sheet at May 31, 2013. The effect of this reclassification is not material to the condensed consolidated financial statements.

Accounting and Disclosure Changes

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2014-09 Revenue from Contracts with Customers (Topic 606). This guidance is intended to improve and converge with international standards the financial reporting requirements for revenue from contracts with customers. It will be effective for our first quarter of 2018 and early adoption is not permitted. We have not yet determined the impact from adoption of this new accounting pronouncement on our financial statements.

In February 2013, the FASB issued Accounting Standards Update No. 2013-02 Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income. This guidance is intended to provide disclosure on items reclassified out of accumulated other comprehensive income (loss) either in the notes or parenthetically on the face of the income statement. We adopted this new accounting pronouncement with our first quarter of 2014 and have included the necessary disclosures in Note 10, Accumulated Other Comprehensive Income (Loss), in this filing. There was no impact on our financial statements from adoption, other than the additional disclosures.

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2. ACQUISITIONS

On May 31, 2013, we completed the purchase of the assets of Wuhan Asia-Pacific Condiments Co. Ltd. (WAPC), a privately held company based in China, for $144.8 million, which included $142.3 million of cash paid, net of closing adjustments, and the assumption of $2.5 million of liabilities. This acquisition was financed with a combination of cash and debt. WAPC manufactures and markets DaQiao and ChuShiLe brand bouillon products, which have a leading position in the central region of China. WAPC is included in our consumer business segment from the date of acquisition. At the time of acquisition, annual sales of WAPC were approximately $122 million. During the second quarter of 2014, we completed the final valuation of the assets of WAPC which resulted in $30.6 million allocated to tangible net assets, $46.1 million allocated to other intangible assets and $68.1 million allocated to goodwill. The completion of the final valuation did not result in material changes to our consolidated income statement or our consolidated balance sheet from our preliminary purchase price allocation. WAPC added $33.8 million and $72.7 million to sales during the three and six months ended May 31, 2014, respectively.
Proforma financial information for this acquisition has not been presented because the financial impact is not material.

3. SPECIAL CHARGES

In the fourth quarter 2013, we announced a reorganization in parts of the Europe, Middle East and Africa (EMEA) region to further improve EMEA's profitability and process standardization while supporting its competitiveness and long-term growth. These actions include the closure of our current sales and distribution operations in The Netherlands, where we will transition to a third-party distributor model to continue to sell the Silvo brand, as well as actions intended to streamline selling, general and administrative activities throughout EMEA, including the centralization of shared service activity across the region into Poland.

We expect to record a total of approximately $27 million of cash and non-cash charges related to this reorganization. For 2013, we recorded $25.0 million of special charges related to this reorganization. We expect to record approximately $2 million of special charges related to this reorganization during 2014 and to complete the actions by 2015. We expect cash expenditures to implement these actions to be approximately $18 million, with the bulk of the spending occurring in 2014, and to realize related annual cost savings of approximately $10 million by 2015. Of the $25.0 million of special charges recognized in 2013, $15.9 million related to employee severance, $6.4 million to asset write-downs, and $2.7 million to other exit costs. The $6.4 million asset write-down in 2013 related to an impairment charge for the reduction in the value of our Silvo brand name in The Netherlands.
The following table outlines the major components of accrual balances relating to the special charges as of November 30, 2013 and May 31, 2014 (in millions):

	Employee severance	Other exit costs	Total
Balance as of November 30, 2013	$15.9	$2.7	$18.6
Amounts utilized	(4.4)	(1.0)	(5.4)
Balance as of May 31, 2014	$11.5	$1.7	$13.2

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4. FINANCING ARRANGEMENTS AND FINANCIAL INSTRUMENTS

We use derivative financial instruments to enhance our ability to manage risk, including foreign currency and interest rate exposures, which exist as part of our ongoing business operations. We do not enter into contracts for trading purposes, nor are we a party to any leveraged derivative instruments. The use of derivative financial instruments is monitored through regular communication with senior management and the use of written guidelines.
As of May 31, 2014, the maximum time frame for our foreign exchange forward contracts is 18 months. For all derivatives, the net amount of accumulated other comprehensive income expected to be reclassified in the next 12 months is $1.0 million as a decrease to earnings.

All derivatives are recognized at fair value in the balance sheet and recorded in either current or noncurrent other assets or other accrued liabilities or other long-term liabilities depending upon nature and maturity.
The following table discloses the fair values of derivative instruments on our balance sheet (in millions):

As of May 31, 2014	Asset Derivatives			Liability Derivatives		
	Balance Sheet Location	Notional Amount	Fair Value	Balance Sheet Location	Notional Amount	Fair Value
Interest rate contracts	Other current assets	$100.0	$9.8			
Foreign exchange contracts	Other current assets	73.8	0.8	Other accrued liabilities	$92.8	$1.4
Total			$10.6			$1.4

As of May 31, 2013	Asset Derivatives			Liability Derivatives		
	Balance Sheet Location	Notional Amount	Fair Value	Balance Sheet Location	Notional Amount	Fair Value
Interest rate contracts	Other current assets	$200.0	$18.4			
Foreign exchange contracts	Other current assets	115.1	1.9	Other accrued liabilities	$64.5	$0.6
Total			$20.3			$0.6

As of November 30, 2013	Asset Derivatives			Liability Derivatives		
	Balance Sheet Location	Notional Amount	Fair Value	Balance Sheet Location	Notional Amount	Fair Value
Interest rate contracts	Other current assets	$100.0	$12.2			
Foreign exchange contracts	Other current assets	79.2	1.1	Other accrued liabilities	$125.7	$1.6
Total			$13.3			$1.6

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The following tables disclose the impact of derivative instruments on our other comprehensive income (OCI), accumulated other comprehensive income (AOCI) and our income statement for the three and six month periods ended May 31, 2014 and 2013 (in millions):

Fair Value Hedges -

Derivative	Income statement location	Expense			
		For the three months ended May 31, 2014	For the three months ended May 31, 2013	For the six months ended May 31, 2014	For the six months ended May 31, 2013
Interest rate contracts	Interest expense	$1.3	$1.3	$2.5	$2.5

Cash Flow Hedges –
For the three months ended May 31,

Derivative	Gain or (Loss) recognized in OCI		Income statement location	Gain or (Loss) reclassified from AOCI	
	2014	2013		2014	2013
Interest rate contracts	—	$3.3	Interest expense	(0.1)	$(0.4)
Foreign exchange contracts	(0.5)	0.6	Cost of goods sold	$(0.1)	(0.2)
Total	$(0.5)	$3.9		$(0.2)	$(0.6)

Cash Flow Hedges –
For the six months ended May 31,

Derivative	Gain or (Loss) recognized in OCI		Income statement location	Gain or (Loss) reclassified from AOCI	
	2014	2013		2014	2013
Interest rate contracts	$—	$4.5	Interest expense	$(0.1)	$(0.7)
Foreign exchange contracts	(0.5)	2.1	Cost of goods sold	(0.5)	(0.7)
Total	$(0.5)	$6.6		$(0.6)	$(1.4)

The amount of gain or loss recognized in income on the ineffective portion of derivative instruments is not material. The amounts noted in the tables above for OCI do not include any adjustments for the impact of deferred income taxes.

5.FAIR VALUE MEASUREMENTS

Fair value can be measured using valuation techniques, such as the market approach (comparable market prices), the income approach (present value of future income or cash flow), and the cost approach (cost to replace the service capacity of an asset or replacement cost). Accounting standards utilize a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The following is a brief description of those three levels:

- Level 1: Observable inputs such as quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets or liabilities in active markets and quoted prices for identical or similar assets or liabilities in markets that are not active.
- Level 3: Unobservable inputs that reflect the reporting entity's own assumptions.

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Our population of financial assets and liabilities subject to fair value measurements on a recurring basis are as follows (in millions):

	May 31, 2014			
	Fair Value	Level 1	Level 2	Level 3
Assets				
Cash and cash equivalents	$81.4	$81.4	$—	$—
Insurance contracts	96.5	—	96.5	—
Bonds and other long-term investments	12.6	12.6	—	—
Interest rate derivatives	9.8	—	9.8	—
Foreign currency derivatives	0.8	—	0.8	—
Total	$201.1	$94.0	$107.1	$—
Liabilities				
Foreign currency derivatives	$1.4	$—	$1.4	$—

	May 31, 2013			
	Fair Value	Level 1	Level 2	Level 3
Assets				
Cash and cash equivalents	$72.1	$72.1	$—	$—
Insurance contracts	80.5	—	80.5	—
Bonds and other long-term investments	13.4	13.4	—	—
Interest rate derivatives	18.4	—	18.4	—
Foreign currency derivatives	1.9	—	1.9	—
Total	$186.3	$85.5	$100.8	$—
Liabilities				
Foreign currency derivatives	$0.6	$—	$0.6	—

	November 30, 2013			
	Fair Value	Level 1	Level 2	Level 3
Assets				
Cash and cash equivalents	$63.0	$63.0	$—	$—
Insurance contracts	90.1	—	90.1	—
Bonds and other long-term investments	13.3	13.3	—	—
Interest rate derivatives	12.2	—	12.2	—
Foreign currency derivatives	1.1	—	1.1	—
Total	$179.7	$76.3	$103.4	$—
Liabilities				
Foreign currency derivatives	$1.6	$—	$1.6	$—

The fair values of insurance contracts are based upon the underlying values of the securities in which they are invested and are from quoted market prices from various stock and bond exchanges for similar type assets. The fair values of bonds and other long-term investments are based on quoted market prices from various stock and bond exchanges. The fair values for interest rate and foreign currency derivatives are based on values for similar instruments using models with market based inputs.

6. EMPLOYEE BENEFIT AND RETIREMENT PLANS

The following table presents the components of our pension expense of the defined benefit plans for the three months ended May 31, 2014 and 2013 (in millions):

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	United States		International	
	2014	2013	2014	2013
Defined benefit plans				
Service cost	$5.0	$5.8	$2.0	$2.2
Interest costs	7.8	7.8	3.4	3.1
Expected return on plan assets	(9.7)	(10.4)	(4.7)	(4.2)
Amortization of prior service costs	—	—	0.1	0.1
Recognized net actuarial loss	2.9	7.4	1.2	1.4
Total pension expense	$6.0	$10.6	$2.0	$2.6

The following table presents the components of our pension expense of the defined benefit plans for the six months ended May 31, 2014 and 2013 (in millions):

	United States		International	
	2014	2013	2014	2013
Defined benefit plans				
Service cost	$10.0	$11.6	$3.9	$4.4
Interest costs	15.6	15.6	6.9	6.3
Expected return on plan assets	(19.4)	(20.7)	(9.4)	(8.5)
Amortization of prior service costs	—	—	0.2	0.2
Recognized net actuarial loss	5.9	14.8	2.3	2.8
Total pension expense	$12.1	$21.3	$3.9	$5.2

During the six months ended May 31, 2014 and 2013, we contributed $11.3 million and $37.7 million, respectively, to our pension plans. Total contributions to our pension plans in fiscal year 2013 were $42.7 million.

The following table presents the components of our other postretirement benefits expense (in millions):

	Three months ended May 31,		Six months ended May 31,	
	2014	2013	2014	2013
Other postretirement benefits				
Service cost	$0.9	$1.2	$1.8	$2.5
Interest costs	1.0	1.0	2.1	2.0
Amortization of prior service costs	—	(0.3)	—	(0.6)
Amortization of losses	—	0.3	—	0.7
Total other postretirement expense	$1.9	$2.2	$3.9	$4.6

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7. STOCK-BASED COMPENSATION

We have three types of stock-based compensation awards: restricted stock units (RSUs), stock options and company stock awarded as part of our mid-term incentive program (MTIP). The following table sets forth the stock-based compensation expense recorded in selling, general and administrative (SG&A) expense (in millions):

	Three months ended May 31,		Six months ended May 31,	
	2014	2013	2014	2013
Stock-based compensation expense	$9.5	$9.7	$12.1	$12.5

Our 2014 annual grant of stock options and RSUs occurred in the second quarter, similar to the 2013 annual grant. The weighted-average grant-date fair value of an option granted in 2014 was $9.48 and in 2013 was $9.47 as calculated under a lattice pricing model. For the 2014 grant, substantially all of the options granted vest ratably over a three-year period or upon retirement. Previously, stock options granted vested ratably over a four-year period or upon retirement. The fair values of option grants in the stated periods were computed using the following range of assumptions for our various stock compensation plans:

	2014	2013
Risk-free interest rates	0.1 - 2.7%	0.1 - 1.8%
Dividend yield	2.1%	1.9%
Expected volatility	15.6 - 20.1%	14.5 - 20.6%
Expected lives	5.8	6.2

The following is a summary of all stock option activity for the six months ended May 31, 2014 and 2013:

	2014			2013		
(shares in millions)	Number of Shares		Weighted-Average Exercise Price	Number of Shares		Weighted-Average Exercise Price
Outstanding at beginning of period	4.6		$47.73	5.1		$40.06
Granted	1.1		71.10	0.9		71.60
Exercised	(0.5	)	35.26	(0.9	)	32.70
Outstanding at end of the period	5.2		$53.54	5.1		$47.13
Exercisable at end of the period	3.0		$44.44	2.9		$38.59

As of May 31, 2014 the intrinsic value (the difference between the exercise price and the market price) for all options outstanding was $97.0 million and for options currently exercisable was $84.2 million. The total intrinsic value of all options exercised during the six months ended May 31, 2014 and 2013 was $17.1 million and $32.7 million, respectively.

The following is a summary of all of our RSU activity for the six months ended May 31, 2014 and 2013:

	2014			2013		
(shares in thousands)	Number of Shares		Weighted-Average Grant-Date Fair Value	Number of Shares		Weighted-Average Grant-Date Fair Value
Outstanding at beginning of period	161		$60.86	192		$49.65
Granted	177		71.14	89		71.60
Vested	(93	)	62.57	(113	)	51.05
Forfeited	(4	)	69.02	(2	)	55.16
Outstanding at end of period	241		$67.61	166		$60.65

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The following is a summary of the MTIP award activity for the six months ended May 31, 2014 and 2013:

(shares in thousands)	2014 Number of Shares	2014 Weighted-Average Grant-Date Fair Value	2013 Number of Shares	2013 Weighted-Average Grant-Date Fair Value
Outstanding at beginning of period	334	$51.73	240	$46.63
Granted	105	69.04	94	64.74
Vested	(118)	44.47	—	—
Forfeited	(2)	44.47	—	—
Outstanding at end of period	319	$60.15	334	$51.73

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8. INCOME TAXES

During the six months ended May 31, 2014, the Company reached a settlement with respect to the French taxing authority's audits of the 2007-2013 tax years. In connection with that settlement, the Company reversed previously provided reserves for uncertain tax benefits and related interest of $5.8 million in the first quarter of 2014. Other than additions for current year tax positions and for the previously described reversal, there were no significant changes to unrecognized tax benefits during the three and six months ended May 31, 2014.

Income taxes for the six months ended May 31, 2014 included the following additional discrete tax items: (i) international tax expense of $2.2 million related to prior year adjustments agreed as part of the French tax settlement previously described; (ii) international tax expense of $3.7 million related to fiscal year 2013 arising from a retroactive change in French tax law enacted in the first quarter; and (iii) international tax expense of $0.6 million relating to an increased valuation allowance associated with prior year losses of a non-U.S. subsidiary due to a change in our assessment of the likely realization of such losses. There were no discrete tax items recognized in the quarter ended May 31, 2014.

Income taxes for the six months ended May 31, 2013 include $1.2 million of discrete tax benefits due to the recognition of a 2012 U.S. research tax credit, which was recorded in the first quarter. A new law was enacted in 2013 that retroactively granted the credit in 2012. There were no discrete tax items recognized in the quarter ended May 31, 2013.

In 2010, the Internal Revenue Service (IRS) commenced an examination of our U.S. federal income tax return for the 2007 and 2008 tax years. During the course of the examination, we have held discussions with the IRS on certain issues and, in October 2012, we received proposed adjustments for these tax years. In November 2012, we deposited $18.8 million with the IRS to stop any potential interest on these proposed adjustments. We disagree with certain of the proposed adjustments and, in December 2012, we filed a protest to initiate the IRS administrative appeals process. In the first two quarters of 2014, the appeals process continued, with meetings and submission of supplemental materials. We believe that we have established appropriate tax accruals under U.S. GAAP for these issues.

9. EARNINGS PER SHARE AND STOCK ISSUANCE

The following table sets forth the reconciliation of average shares outstanding (in millions):

	Three months ended May 31,		Six months ended May 31,	
	2014	2013	2014	2013
Average shares outstanding – basic	130.2	132.1	130.6	132.3
Effect of dilutive securities:				
Stock options/RSUs/MTIP	1.0	1.5	1.1	1.5
Average shares outstanding – diluted	131.2	133.6	131.7	133.8

The following table sets forth the stock options and RSUs for the three and six months ended May 31, 2014 and 2013 which were not considered in our earnings per share calculation since they were anti-dilutive (in millions):

	Three months ended May 31,		Six months ended May 31,	
	2014	2013	2014	2013
Anti-dilutive securities	1.6	0.3	1.3	0.3

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The following table sets forth the common stock activity for the six months ended May 31, 2014 and 2013 under the Company’s stock option and employee stock purchase plans and the repurchases of common stock under its stock repurchase program (in millions):

	Three months ended May 31,		Six months ended May 31,	
	2014	2013	2014	2013
Shares issued under stock option, employee stock purchase plans and RSUs	0.3	0.5	0.6	0.9
Shares repurchased in connection with the stock repurchase program	1.0	0.4	1.9	1.4

As of May 31, 2014, $234 million remained of the $400 million share repurchase authorization that was authorized by the Board of Directors in April 2013.

10. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The following table sets forth the components of accumulated other comprehensive income (loss), net of tax where applicable (in millions):

	May 31, 2014	May 31, 2013	November 30, 2013
Foreign currency translation adjustment	$169.8	$120.6	$165.7
Unrealized gain (loss) on foreign currency exchange contracts	(0.3)	0.3	(0.3)
Fair value of open interest rate swaps	—	4.3	—
Unamortized value of settled interest rate swaps	1.9	(4.9)	2.0
Pension and other postretirement costs	(162.6)	(304.5)	(167.7)
Accumulated other comprehensive income (loss)	$8.8	$(184.2)	$(0.3)

The following table sets forth the amounts reclassified from accumulated other comprehensive income (loss) and into consolidated net income for the three and six months ended May 31, 2014 and 2013 (in millions):

Accumulated Other Comprehensive Income (Loss) Components	Three months ended May 31, 2014	Three months ended May 31, 2013	Six months ended May 31, 2014	Six months ended May 31, 2013	Affected Line Items in the Condensed Consolidated Income Statement
Losses on cash flow hedges:					
Interest rate derivatives	(0.1)	$(0.4)	$(0.1)	$(0.7)	Interest expense
Foreign exchange contracts	$(0.1)	(0.2)	(0.5)	(0.7)	Cost of goods sold
Total before tax expense	(0.2)	(0.6)	(0.6)	(1.4)	
Tax effect	0.1	0.2	0.2	0.4	Income taxes
Net, after tax	$(0.1)	$(0.4)	$(0.4)	$(1.0)	
Amortization of pension and postretirement benefit adjustments:					
Amortization of prior service costs (1)	$0.1	$(0.2)	$0.2	$(0.4)	SG&A expense/ Cost of goods sold
Amortization of net actuarial losses (1)	4.1	9.1	8.2	18.3	SG&A expense/ Cost of goods sold
Total before tax expense	4.2	8.9	8.4	17.9	
Tax effect	(1.4)	(3.0)	(2.9)	(6.1)	Income taxes
Net, after tax	$2.8	$5.9	$5.5	$11.8	

(1) This accumulated other comprehensive income (loss) component is included in the computation of total pension expense and total other postretirement expense (refer to note 6 for additional details).

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11. BUSINESS SEGMENTS

We operate in two business segments: consumer and industrial. The consumer and industrial segments manufacture, market and distribute spices, herbs, seasoning mixes, condiments and other flavorful products throughout the world. Our consumer segment sells to retail outlets, including grocery, mass merchandise, warehouse clubs, discount and drug stores under the “McCormick” brand and a variety of brands around the world, including “Lawry’s”, “Zatarain’s”, “Simply Asia”, “Thai Kitchen”, “Ducros”, “Vahine”, “Schwartz”, “Club House”, “Kamis”, “Kohinoor” and "DaQiao". Our ind segment sells to food manufacturers and the foodservice industry both directly and indirectly through distributors.
In each of our segments, we produce and sell many individual products which are similar in composition and nature. With their primary attribute being flavor, we regard the products within each of our segments to be fairly homogenous. It is impracticable to segregate and identify sales and profits for individual product lines.
We measure segment performance based on operating income. Although the segments are managed separately due to their distinct distribution channels and marketing strategies, manufacturing and warehousing are often integrated to maximize cost efficiencies. We do not segregate jointly utilized assets by individual segment for internal reporting, evaluating performance or allocating capital. Because of manufacturing integration for certain products within the segments, products are not sold from one segment to another but rather inventory is transferred at cost. Intersegment sales are not material.

	Consumer	Industrial (in millions)	Total
Three months ended May 31, 2014			
Net sales	$615.0	$418.4	$1,033.4
Operating income	85.8	35.9	121.7
Income from unconsolidated operations	6.0	0.2	6.2
Three months ended May 31, 2013			
Net sales	$591.0	$411.6	$1,002.6
Operating income	87.6	28.4	116.0
Income from unconsolidated operations	5.3	0.6	5.9

	Consumer	Industrial (in millions)	Total
Six months ended May 31, 2014			
Net sales	$1,230.3	$796.5	$2,026.8
Operating income	180.2	66.1	246.3
Income from unconsolidated operations	10.9	0.4	11.3
Six months ended May 31, 2013			
Net sales	$1,160.7	$776.2	$1,936.9
Operating income	175.3	52.7	228.0
Income from unconsolidated operations	9.9	1.5	11.4

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

OVERVIEW

Our Business

We are a global leader in flavor, with the manufacturing, marketing and distribution of spices, seasoning mixes, condiments and other flavorful products to the entire food industry. Customers range from retail outlets and food manufacturers to food service businesses. Our major sales, distribution and production facilities are located in North America, Europe and China. Additional facilities are based in Australia, Mexico, India, Singapore, Central America, Thailand and South Africa. Annually, approximately 40% of our sales have been outside of the United States.

We operate in two business segments, consumer and industrial. Consistent with market conditions in each segment, our consumer business has a higher overall profit margin than our industrial business. Historically, the consumer business contributes approximately 60% of sales and 80% of operating income and the industrial business contributes approximately 40% of sales and 20% of operating income. Across both segments, we have the customer base and product breadth to participate in all types of eating occasions, whether it is cooking at home, dining out, purchasing a quick service meal or enjoying a snack. We offer consumers a range of products from premium to value-priced.

Our Growth Model and Outlook

Our growth model is straightforward – we are increasing sales and profits by investing in the business and funding these investments, in part, with cost savings from our Comprehensive Continuous Improvement (CCI) program. This simple model has been the driver of our success and is our plan for growth in the future.

Increasing Sales and Profits – Our long-term goals are to grow sales 4% to 6%, increase operating income 7% to 9% and increase earnings per share 9% to 11%. Long-term, we expect to achieve our sales growth with one-third from category growth, share gains and new distribution, one-third from product innovation and one-third from acquisitions. For our consumer business, we are driving sales with a robust pipeline of innovation and a significant increase in our brand marketing. We expect to increase industrial business sales and profit through new product development and support for the international expansion of our customers.

In 2014, sales are projected to grow 3% to 5% in local currency, driven by higher volumes, pricing and the incremental impact of the WAPC acquisition in the first half of the year (see note 2 of the financial statements for additional information). Operating income was $550.5 million in fiscal year 2013. Excluding special charges of $25.0 million re