

USG CORP  
Form DEFA14A  
April 13, 2018

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

SCHEDULE 14A

Proxy Statement Pursuant to Section 14(a) of  
the Securities Exchange Act of 1934 (Amendment No. )

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

- Preliminary Proxy Statement
- Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))
- Definitive Proxy Statement
- Definitive Additional Materials
- Soliciting Material under §240.14a-12

USG CORPORATION  
(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

- No fee required.
- Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

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Filed herewith as Exhibit 1 is an updated letter to the Company's stockholders that includes information regarding the Company's proxy solicitor D.F. King.

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EXHIBIT 1

Dear Fellow Stockholder,

Recently, Gebr. Knauf KG, a private German company which is a 10.5% stockholder in USG and a competitor in the global gypsum market, sent an open letter to all USG stockholders asking you to vote against four USG Board nominees who are up for election at the upcoming Annual Meeting of Stockholders on May 9, 2018. This is a misguided attempt to pressure the Board into accepting a proposal from Knauf to purchase USG, that we believe is substantially below our intrinsic value. The Board will not yield to this pressure and is committed to acting in the best interests of all USG stockholders even in the face of Knauf's campaign.

The Board is committed to creating value for all our stockholders through the execution of our strategic plan, which we outlined at our recent Investor Day. While the Board has not made the decision to sell the Company, it remains open to the evaluation of any proposal to acquire USG, as it has done with Knauf's proposals. If Knauf, or any other viable bidder, makes a proposal that reflects the Company's intrinsic value, the Board would seek to negotiate an appropriate confidentiality arrangement to allow it to share information with the potential counterparty. The USG Board has declined to share confidential information with Knauf because, in addition to being a competitor, Knauf's acquisition proposal is not at a value that the Board believes adequately compensates all stockholders.

To be clear – Knauf's campaign is designed to undermine the Board's ability to maximize value for all stockholders.

This vote, which has no legal bearing on any corporate action or the retention of the incumbent directors, only serves as a propaganda tool for a competitor who is unwilling to pay an appropriate value for your Company.

**VOTE THE WHITE PROXY CARD "FOR" THE ELECTION OF USG'S HIGHLY QUALIFIED  
INDEPENDENT DIRECTORS**

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**OUR BOARD HAS ENGAGED REPEATEDLY WITH KNAUF AND IS ACTING IN THE BEST INTERESTS OF ALL STOCKHOLDERS**

Since Knauf's first approach, our Board has engaged with them in good faith and has carefully evaluated their proposals – Knauf would have you believe that is not the case and has made disingenuous and misleading public statements regarding the Company's level of engagement. To set the record straight:

• On November 29, 2017, Knauf first proposed to acquire USG for \$40.10 per share, which represented a 9% premium to our prior day closing stock price.

• After careful evaluation, our Board rejected this proposal and USG management subsequently spoke with Knauf to explain the Board's rationale and elements that impact USG's intrinsic value.

• Our stock traded as high as \$41.18 in January 2018 – unaffected by public takeover speculation.

• On March 8, 2018, we held our Investor Day (which had been under development since mid-2017), where we outlined our strategy – Knauf representatives attended in person.

• On March 12, 2018, at Knauf's request, Steven Leer, our non-executive Chairman and Jennifer Scanlon, our CEO, met with Alexander Knauf and Manfred Grunke, Knauf's Managing Partners, in person.

• Three days later, Knauf submitted its revised proposal of \$42.00 per share, which was then only a 2% premium to our recent 52-week high.

Our Board again carefully considered and rejected this revised proposal on the basis of USG's intrinsic value, which has been increased by the materially positive impact of the reduction to U.S. corporate tax rates, which had been signed into law after the initial Knauf proposal.

• On March 26, 2018, in connection with a letter outlining the rationale for the rejection of Knauf's offer, we suggested a further call with Knauf's leadership team, which took place on March 29, 2018.

• Following the March 29, 2018, call, the Board directed USG's financial and legal advisors to meet in person with advisors from Knauf, which took place on April 5, 2018.

• On April 10, 2018, Knauf issued a letter to USG stockholders claiming – among other things – that the USG Board did not engage in good faith with them. This is clearly not true.

**KNAUF HAS DISREGARDED THE FACT THAT USG IS A TRANSFORMED COMPANY POISED TO DELIVER SIGNIFICANT VALUE**

Knauf's letter to USG stockholders focuses on a decade-old history of USG, which includes the period of the great recession and housing bubble, and is completely irrelevant to where the Company is positioned today. The reality is that our Board and management team have completely transformed our company, most significantly in the last two years, resulting in a drastically improved cost position, profitability, capital structure and portfolio.

As an example of 10 years of dramatic change, consider that our 2017 Adjusted Operating Profit was approximately two times greater than our 2007 Adjusted Operating Profit, with housing starts approximately 11 percent lower. Knauf is well aware of these facts and is trying to mislead you.

• More recently, the last five years have shown significant improvements across key USG financial metrics:



Value Driver	Measure	2012	2017	Change	Future Value Upside
Profitability	Adjusted Operating Profit <sup>(1)</sup>	\$91M	\$438M	+\$347M / +381%	Significant operating leverage with increased mid-cycle earnings
	Adjusted Operating Margin <sup>(1)</sup>	4%	14%	+1,000bps	
	Total Debt	\$2,309M	\$1,089M	-\$1,220M	
Capital Structure	Interest Expense	\$206M	\$69M	-\$137M	Balance sheet flexibility to fund growth and return capital
	Leverage <sup>(2)</sup>	9.5x	1.8x	-7.7x	
	Share Repurchases	\$0M	\$184M	+\$184M	
Portfolio	Business and Geographic Mix	North America & Europe Manufacturing & Distribution	North America, Asia, Australasia, and Middle East Manufacturing	Exposure to Asia & Australasia; exited Europe and South America	Stronger growth profile and reduced cyclicality

1. Non-GAAP Metric. See reconciliation to GAAP results in the Appendix.

2. Non-GAAP Metric. Net adjusted debt/adjusted EBITDA. See reconciliation to GAAP results in the Appendix.

USG is now a pure manufacturer with an enhanced portfolio and greater exposure to the highest growth construction markets in the world. This transformation has positioned us for significant growth and value creation ahead.

#### USG HAS PIVOTED TO A NEW STRATEGY THAT WE ARE CONFIDENT WILL CREATE LONG-TERM VALUE FOR ALL OUR STOCKHOLDERS

Knauf indicates their proposal “de-risks” any future business plan – the reality is their proposal would prohibit all USG stockholders from sharing in the benefits of USG’s strategic plan, which positions the Company to drive meaningful financial and operational improvements, including significant margin expansion and more than double our 2017 free cash flow by 2020. Other key strategy elements include:

Our favorable cost position is improving further through advanced manufacturing, which we expect to deliver \$100M of run-rate EBITDA by the end of 2020. Our advanced manufacturing initiatives and other cost efficiency efforts are powerful levers that are independent of market conditions and are already funded in our plan.

Recent innovative product launches are gaining meaningful traction due to strong customer demand, and are expected to deliver significant upside over the next few years. Exciting additional new products are in our pipeline.

These innovations drive continued differentiation and support USG’s price premium in the market.

As reflected in the chart below, management expects its strategy to result in improved adjusted operating profit margin.

¶ This clear potential is, in part, why we view Knauf's proposal as opportunistic.

Knauf is attempting to scare USG stockholders by claiming we will have to make significant capital investments, but in fact significant investments have been and are being made, and we expect to generate more than enough cash to fund capex needs in the coming years while also retaining the ability to return capital to stockholders.

**THE HIGHLY SUPPORTIVE MACROECONOMIC ENVIRONMENT IS EXPECTED TO FURTHER ACCELERATE THE BENEFITS OF USG'S STRATEGY**

Knauf's focus on industry cyclicalities and cycle timing is another attempt to obscure observable market data: While there has been modest growth in this recovery, key industry indicators still meaningfully lag long-term means. We continue to believe significant industry upside remains in residential and non-residential starts and repair and remodel activity.

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Our transformation, including the sale of our distribution business, expansion into Asia, Australasia and the Middle East, and reduction of debt, has dampened out our cyclical. In addition, the initiatives underway will drive meaningful value regardless of where we are in the cycle.

**THE STRATEGIC VALUE OF USG TO KNAUF IS SUBSTANTIAL AND THEY ARE NOT COMPENSATING ALL STOCKHOLDERS**

Knauf is a private German company which has been in existence for 86 years, with stated net sales in excess of \$8 billion and EBITDA in excess of \$1.6 billion. While Knauf has operations in many regions of the world, it does not have a significant presence in North America and, in particular, the U.S. gypsum market.

Knauf stands to benefit substantially from a combination with USG, as its proposals reference “compelling strategic logic” and its principals acknowledged its expectation of meaningful synergies for Knauf.

USG’s #1 market position in North America and industry leading technology, patents and brands, such as our Sheetrock® brand, make us the “crown jewel” of the industry, and we are critical for Knauf to achieve their goal of being the global leader in wallboard.

Indeed, it is this technology and intellectual property portfolio that Boral sought and placed a high value on in the formation in 2014 of our highly successful USG Boral joint venture.

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SEND A STRONG MESSAGE THAT YOU SUPPORT OUR BOARD'S EFFORTS TO  
MAXIMIZE VALUE FOR ALL STOCKHOLDERS

VOTE THE WHITE PROXY CARD "FOR"  
THE RE-ELECTION OF USG'S STRONG BOARD TODAY

Vote the WHITE card "FOR" the re-election of USG's highly qualified and experienced director nominees: Jose Armario, Gretchen R. Haggerty and William H. Hernandez and our new director nominee: Dana S. Cho.

Your Board and management team have successfully transformed USG to position the Company for the significant opportunities ahead. We are confident that we have the right strategy, the right management team and the right Board of Directors in place to continue delivering value for all USG stockholders.

Your vote is important and we strongly urge you to protect your investment by voting "FOR" on the white card today.

On behalf of USG's Board of Directors, we thank you for your ongoing support, and look forward to continued engagement.

Sincerely,

USG Board of Directors

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#### Appendix of Non-GAAP Financial Measures

In this letter, the Company's financial results are provided both in accordance with accounting principles generally accepted in the United States of America (GAAP) and using certain non-GAAP financial measures. In particular, the Company presents the non-GAAP financial measures adjusted operating profit and margin, free cash flow, EBITDA and leverage ratio, which exclude certain items. The non-GAAP financial measures are included as a complement to results provided in accordance with GAAP because management believes these non-GAAP financial measures help investors' ability to analyze underlying trends in the Company's business, evaluate its performance relative to other companies in its industry and provide useful information to both management and investors by excluding certain items that may not be indicative of the Company's core operating results. Adjusted operating profit includes the equity method income from USG Boral Building Products (UBBP) and USG's income from other equity investments because management views UBBP and its other equity investments as important businesses. In addition, the Company uses adjusted operating profit and adjusted operating margins as components in the measurement of incentive compensation. The non-GAAP measures should not be considered a substitute for or superior to GAAP results and may vary from others in the industry. For further information related to the Company's use of non-GAAP financial measures, and reconciliations to the nearest GAAP measures, see the Appendix.

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## Adjusted Operating Profit Reconciled to GAAP Operating Profit under New Reportable Segments

\$ Millions	FY 2017
Reported GAAP Operating Profit (Loss)	
U.S. Wallboard and Surfaces	\$314
U.S. Performance Materials	\$26
U.S. Ceilings	\$95
Canada	\$12
Other	\$11
Corporate & Eliminations	(\$91)
Total	\$367
Adjustments to GAAP Operating Profit (Loss)	
U.S. Wallboard and Surfaces – Pension settlement charge	\$7
U.S. Performance Materials – Pension settlement charge	\$2
U.S. Ceilings – Pension settlement charge	\$2
Corporate & Eliminations – Pension settlement charge	\$1
Total	\$12
Adjusted Operating Profit (Loss) – Non-GAAP measure	
U.S. Wallboard and Surfaces	\$321
U.S. Performance Materials	\$28
U.S. Ceilings	\$97
Canada	\$12
Other	\$11
Corporate & Eliminations	(\$90)
Other Adjustments	
Adjusted equity income from UBBP	\$59
Total Adjusted Operating Profit	\$438

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## Adjusted Operating Profit Recast for Change in Employee Retirement Plan Accounting

\$ Millions	FY 2017 AOP %	
Reported Adjusted Operating Profit (Loss) – Non GAAP Measure		
U.S. Wallboard and Surfaces	\$321	16.8%
U.S. Performance Materials	\$28	7.5%
U.S. Ceilings	\$97	20.3%
Canada	\$12	3.0%
Other	\$11	
Corporate & Eliminations	(\$90)	
Adjusted equity income from UBBP	\$59	
Total	\$438	13.7%
Adjustments to Adjusted Operating Profit (Loss)		
U.S. Wallboard and Surfaces – Employee Retirement Plan Accounting Change	(\$15)	
U.S. Performance Materials – Employee Retirement Plan Accounting Change	(\$4)	
U.S. Ceilings – Employee Retirement Plan Accounting Change	(\$5)	
Canada – Employee Retirement Plan Accounting Change	\$1	
Corporate & Eliminations – Employee Retirement Plan Accounting Change	(\$3)	
Total	(\$26)	
Recasted Adjusted Operating Profit (Loss) – Non-GAAP measure		
U.S. Wallboard and Surfaces	\$306	16.0%
U.S. Performance Materials	\$24	6.4%
U.S. Ceilings	\$92	19.3%
Canada	\$13	3.2%
Other	\$11	
Corporate & Eliminations	(\$93)	
Adjusted equity income from UBBP	\$59	
Total Adjusted Operating Profit	\$412	12.9%

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GAAP Operating P