
**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 the quarterly period ended March 31, 2014

or

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

For the transition period from _____ to _____

Commission file number 1-5667

Cabot Corporation

(Exact name of registrant as specified in its charter)

Delaware
(State of Incorporation)

04-2271897
(I.R.S. Employer
Identification No.)

Two Seaport Lane
Boston, Massachusetts
(Address of principal executive offices)

02210-2019
(Zip Code)

Registrant's telephone number, including area code: (617) 345-0100

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 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 (§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 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 definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if smaller reporting company) 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

Indicate the number of shares outstanding of each of the issuer's classes of Common Stock, as of the latest practicable date.

As of May 1, 2014 the Company had 64,485,689 shares of Common Stock, par value \$1.00 per share, outstanding.

CABOT CORPORATION

INDEX

Part I. [Financial Information](#)

| | | |
|---------|---|----|
| Item 1. | Financial Statements (unaudited) | |
| | Consolidated Statements of Operations for the Three and Six Months Ended March 31, 2014 and 2013 | 3 |
| | Consolidated Statements of Comprehensive Income (Loss) for the Three and Six Months Ended March 31, 2014 and 2013 | 4 |
| | Consolidated Balance Sheets as of March 31, 2014 and September 30, 2013 | 5 |
| | Consolidated Statements of Cash Flows for the Six Months Ended March 31, 2014 and 2013 | 7 |
| | Notes to Consolidated Financial Statements | 8 |
| Item | | |
| 2. | Management's Discussion and Analysis of Financial Condition and Results of Operations | 32 |
| Item | | |
| 3. | Quantitative and Qualitative Disclosures About Market Risk | 48 |
| Item | | |
| 4. | Controls and Procedures | 48 |

Part II. [Other Information](#)

| | | |
|---------|---|----|
| Item 1. | Legal Proceedings | 48 |
| Item | | |
| 2. | Unregistered Sales of Equity Securities and Use of Proceeds | 49 |
| Item | | |
| 6. | Exhibits | 50 |

[Table of Contents](#)

Part I. Financial Information

Item 1. Financial Statements

**CABOT CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS
UNAUDITED**

| | <u>Three Months Ended March 31</u> | | <u>Six Months Ended March 31</u> | |
|--|---|----------------|----------------------------------|----------------|
| | 2014 | 2013 | 2014 | 2013 |
| | (In millions, except share and per share amounts) | | | |
| Net sales and other operating revenues | \$ 898 | \$ 840 | \$ 1,796 | \$ 1,659 |
| Cost of sales | 722 | 697 | 1,441 | 1,369 |
| Gross profit | 176 | 143 | 355 | 290 |
| Selling and administrative expenses | 92 | 77 | 169 | 150 |
| Research and technical expenses | 16 | 16 | 31 | 33 |
| Income from operations | 68 | 50 | 155 | 107 |
| Interest and dividend income | 1 | 1 | 2 | 2 |
| Interest expense | (13) | (16) | (27) | (32) |
| Other (expense) income | (8) | 2 | 27 | 3 |
| Income from continuing operations before income taxes and equity in earnings of affiliated companies | 48 | 37 | 157 | 80 |
| Provision for income taxes | (7) | (16) | (31) | (36) |
| Equity in (loss) earnings of affiliated companies, net of tax | (2) | 3 | — | 6 |
| Income from continuing operations | 39 | 24 | 126 | 50 |
| Loss from discontinued operations, net of tax | — | (1) | (1) | (3) |
| Net income | 39 | 23 | 125 | 47 |
| Net income (loss) attributable to noncontrolling interests, net of tax | 3 | (4) | 9 | — |
| Net income attributable to Cabot Corporation | <u>\$ 36</u> | <u>\$ 27</u> | <u>\$ 116</u> | <u>\$ 47</u> |
| Weighted-average common shares outstanding, in millions: | | | | |
| Basic | 64.4 | 63.7 | 64.2 | 63.6 |
| Diluted | 65.1 | 64.4 | 65.0 | 64.3 |
| Income per common share: | | | | |
| Basic: | | | | |
| Income from continuing operations attributable to Cabot Corporation | \$ 0.56 | \$ 0.44 | \$ 1.81 | \$ 0.79 |
| Loss from discontinued operations | (0.01) | (0.01) | (0.02) | (0.05) |
| Net income attributable to Cabot Corporation | <u>\$ 0.55</u> | <u>\$ 0.43</u> | <u>\$ 1.79</u> | <u>\$ 0.74</u> |
| Diluted: | | | | |
| Income from continuing operations attributable to Cabot Corporation | \$ 0.55 | \$ 0.43 | \$ 1.79 | \$ 0.78 |
| Loss from discontinued operations | (0.01) | (0.01) | (0.02) | (0.05) |
| Net income attributable to Cabot Corporation | <u>\$ 0.54</u> | <u>\$ 0.42</u> | <u>\$ 1.77</u> | <u>\$ 0.73</u> |
| Dividends per common share | <u>\$ 0.20</u> | <u>\$ 0.20</u> | <u>\$ 0.40</u> | <u>\$ 0.40</u> |

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

CABOT CORPORATION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
UNAUDITED

| | <u>Three Months Ended March 31</u> | | <u>Six Months Ended March 31</u> | |
|---|------------------------------------|-------------|----------------------------------|-------------|
| | <u>2014</u> | <u>2013</u> | <u>2014</u> | <u>2013</u> |
| | (In millions) | | | |
| Net income | \$ 39 | \$ 23 | \$ 125 | \$ 47 |
| Other comprehensive loss, net of tax | | | | |
| Foreign currency translation adjustment (net of tax of benefit of \$-, \$7, \$1 and \$14) | (8) | (36) | (29) | (22) |
| Unrealized holding gains arising during the period (net of tax of less than \$1 million in all periods) | — | 1 | — | 1 |
| Pension and other postretirement credit liability adjustments | | | | |
| Pension and other postretirement benefit liability adjustments arising during the period (net of tax of less than \$1 million in all periods) | — | 2 | — | 2 |
| Amortization of net loss and prior service credit included in net periodic pension cost (net of tax benefit of \$-, \$1, \$- and \$-) | 1 | — | 1 | 1 |
| Other comprehensive loss | (7) | (33) | (28) | (18) |
| Comprehensive income (loss) | 32 | (10) | 97 | 29 |
| Net income (loss) attributable to noncontrolling interests | 3 | (4) | 9 | — |
| Noncontrolling interests foreign currency translation adjustment, net of tax | (1) | (1) | (2) | — |
| Comprehensive income (loss) attributable to noncontrolling interests, net of tax | 2 | (5) | 7 | — |
| Comprehensive income (loss) attributable to Cabot Corporation | \$ 30 | \$ (5) | \$ 90 | \$ 29 |

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

CABOT CORPORATION
CONSOLIDATED BALANCE SHEETS
ASSETS
UNAUDITED

| | March 31, 2014 | September 30, 2013 |
|---|-------------------|-----------------------|
| | (In millions) | |
| Current assets: | | |
| Cash and cash equivalents | \$ 89 | \$ 95 |
| Accounts and notes receivable, net of reserve for doubtful accounts of \$11 and \$8 | 712 | 634 |
| Inventories: | | |
| Raw materials | 129 | 100 |
| Work in process | 3 | 2 |
| Finished goods | 364 | 309 |
| Other | 45 | 44 |
| Total inventories | 541 | 455 |
| Prepaid expenses and other current assets | 94 | 58 |
| Notes receivable from sale of business | 215 | 214 |
| Deferred income taxes | 34 | 36 |
| Current assets held for sale | 3 | 3 |
| Total current assets | <u>1,688</u> | <u>1,495</u> |
| Property, plant and equipment, net | 1,617 | 1,600 |
| Goodwill | 555 | 502 |
| Equity affiliates | 73 | 119 |
| Intangible assets, net | 358 | 308 |
| Assets held for rent | 55 | 49 |
| Deferred income taxes | 75 | 68 |
| Other assets | 58 | 83 |
| Noncurrent assets held for sale | 8 | 9 |
| Total assets | <u>\$ 4,487</u> | <u>\$ 4,233</u> |

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

**CABOT CORPORATION
CONSOLIDATED BALANCE SHEETS
LIABILITIES AND STOCKHOLDERS' EQUITY
UNAUDITED**

| | March 31, 2014 | September 30, 2013 |
|--|--|-----------------------|
| | (In millions, except share and per share amounts) | |
| Current liabilities: | | |
| Notes payable | \$ 377 | \$ 264 |
| Accounts payable and accrued liabilities | 528 | 534 |
| Income taxes payable | 35 | 30 |
| Deferred income taxes | 3 | 2 |
| Current portion of long-term debt | 19 | 14 |
| Total current liabilities | <u>962</u> | <u>844</u> |
| Long-term debt | 1,023 | 1,020 |
| Deferred income taxes | 51 | 21 |
| Other liabilities | 273 | 265 |
| Redeemable preferred stock | 29 | — |
| Commitments and contingencies (Note I) | | |
| Stockholders' equity: | | |
| Preferred stock: | | |
| Authorized: 2,000,000 shares of \$1 par value | | |
| Issued and Outstanding : None and none | — | — |
| Common stock: | | |
| Authorized: 200,000,000 shares of \$1 par value | | |
| Issued: 64,723,232 and 64,223,985 shares | | |
| Outstanding: 64,470,691 and 63,970,502 shares | 65 | 64 |
| Less cost of 252,541 and 253,483 shares of common treasury stock | (8) | (8) |
| Additional paid-in capital | 51 | 39 |
| Retained earnings | 1,845 | 1,755 |
| Deferred employee benefits | — | (2) |
| Accumulated other comprehensive income | 77 | 103 |
| Total Cabot Corporation stockholders' equity | <u>2,030</u> | <u>1,951</u> |
| Noncontrolling interests | 119 | 132 |
| Total stockholders' equity | <u>2,149</u> | <u>2,083</u> |
| Total liabilities and stockholders' equity | <u>\$ 4,487</u> | <u>\$ 4,233</u> |

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

CABOT CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
UNAUDITED

| | Six Months Ended March 31 | |
|---|------------------------------|--------------|
| | 2014 | 2013 |
| | (In millions) | |
| Cash Flows from Operating Activities: | | |
| Net income | \$ 125 | \$ 47 |
| Adjustments to reconcile net income to cash provided by operating activities: | | |
| Depreciation and amortization | 100 | 99 |
| Impairment of assets | 3 | 16 |
| Deferred tax provision | (3) | 7 |
| Gain on existing investment in NHUMO | (29) | — |
| Loss on disposal of property, plant and equipment | 2 | 2 |
| Equity in earnings of affiliated companies | — | (6) |
| Non-cash compensation | 8 | 10 |
| Other | (2) | 2 |
| Changes in assets and liabilities: | | |
| Accounts and notes receivable | (52) | (8) |
| Inventories | (76) | (43) |
| Prepaid expenses and other current assets | (15) | (16) |
| Accounts payable and accrued liabilities | (14) | (74) |
| Income taxes payable | 1 | (30) |
| Other liabilities | 4 | (5) |
| Cash dividends received from equity affiliates | 21 | 6 |
| Other | (4) | (3) |
| Cash provided by operating activities | <u>69</u> | <u>4</u> |
| Cash Flows from Investing Activities: | | |
| Additions to property, plant and equipment | (70) | (127) |
| Receipts from notes receivable from sale of business | — | 30 |
| Change in assets held for rent | (5) | (4) |
| Cash paid for acquisition of business, net of cash acquired of \$7 | (73) | — |
| Cash used in investing activities | <u>(148)</u> | <u>(101)</u> |
| Cash Flows from Financing Activities: | | |
| Borrowings under financing arrangements | 13 | 6 |
| Repayments under financing arrangements | (6) | (8) |
| Proceeds from long-term debt, net of issuance costs | 15 | 94 |
| Repayments of long-term debt | (7) | (263) |
| Increase in notes payable, net | (5) | 8 |
| Proceeds from issuance of commercial paper, net | 111 | 256 |
| Proceeds from cash contributions received from noncontrolling stockholders | — | 9 |
| Purchases of common stock | (6) | (6) |
| Proceeds from sales of common stock | 10 | 5 |
| Cash dividends paid to noncontrolling interests | (10) | (6) |
| Cash dividends paid to common stockholders | <u>(26)</u> | <u>(26)</u> |
| Cash provided by financing activities | <u>89</u> | <u>69</u> |
| Effect of exchange rate changes on cash | <u>(16)</u> | <u>(7)</u> |
| Decrease in cash and cash equivalents | (6) | (35) |
| Cash and cash equivalents at beginning of period | 95 | 120 |
| Cash and cash equivalents at end of period | <u>\$ 89</u> | <u>\$ 85</u> |

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

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

A. Basis of Presentation

The consolidated financial statements include the accounts of Cabot Corporation (“Cabot” or the “Company”) and its wholly owned subsidiaries and majority-owned and controlled U.S. and non-U.S. subsidiaries. Additionally, Cabot considers consolidation of entities over which control is achieved through means other than voting rights, of which there were none in the periods presented. Intercompany transactions have been eliminated in consolidation.

The unaudited consolidated financial statements have been prepared in accordance with the requirements of Form 10-Q and consequently do not include all disclosures required by Form 10-K. Additional information may be obtained by referring to Cabot’s Annual Report on Form 10-K for the fiscal year ended September 30, 2013 (“2013 10-K”).

The financial information submitted herewith is unaudited and reflects all adjustments which are, in the opinion of management, necessary to provide a fair statement of the results for the interim periods ended March 31, 2014 and 2013. All such adjustments are of a normal recurring nature. The results for interim periods are not necessarily indicative of the results to be expected for the fiscal year.

In November 2013, the Company purchased all of Grupo Kuo S.A.B. de C.V.’s (“KUO”) common stock in NHUMO, S.A. de C.V. (“NHUMO”), a carbon black joint venture between the Company and KUO in Mexico, which represented approximately 60% of the outstanding common stock of NHUMO (the “NHUMO transaction”). Prior to this transaction, the Company owned approximately 40% of the outstanding common stock of NHUMO, and the NHUMO entity was accounted for as an equity affiliate of the Company. The financial position, results of operations and cash flows of NHUMO are included in the Company’s consolidated financial statements from the date of acquisition.

In March 2014, the Company entered into an agreement to sell its Security Materials business to SICPA SA (“SICPA”). The business is being accounted for as discontinued operations and the applicable assets of the business have been classified as held for sale in the Consolidated Balance Sheets as of March 31, 2014 and September 30, 2013. The Consolidated Statements of Operations for all periods presented have been recast to reflect the Security Materials business in discontinued operations. Unless otherwise indicated, all disclosures and amounts in the Notes to Consolidated Financial Statements relate to the Company’s continuing operations.

B. Significant Accounting Policies***Revenue Recognition and Accounts Receivable***

Cabot recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price is fixed or determinable and collectability is reasonably assured. Cabot generally is able to ensure that products meet customer specifications prior to shipment. If the Company is unable to determine that the product has met the specified objective criteria prior to shipment or if title has not transferred because of sales terms, the revenue is considered “unearned” and is deferred until the revenue recognition criteria are met.

Shipping and handling charges related to sales transactions are recorded as sales revenue when billed to customers or included in the sales price.

The following table shows the relative size of the revenue recognized in each of the Company’s reportable segments for the periods presented. The Advanced Technologies reportable segment excludes the Security Materials business from all periods as the Company began reporting the business under discontinued operations.

| | Three Months Ended | | Six Months Ended | |
|-------------------------|---------------------------|-------------|-------------------------|-------------|
| | March 31 | | March 31 | |
| | 2014 | 2013 | 2014 | 2013 |
| Reinforcement Materials | 58% | 56% | 58% | 58% |
| Performance Materials | 28% | 30% | 27% | 27% |
| Purification Solutions | 9% | 9% | 9% | 10% |
| Advanced Technologies | 5% | 5% | 6% | 5% |

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

Cabot derives the substantial majority of its revenues from the sale of products in Reinforcement Materials and Performance Materials. Revenue from these products is typically recognized when the product is shipped and title and risk of loss have passed to the customer. The Company offers certain of its customers cash discounts and volume rebates as sales incentives. The discounts and volume rebates are recorded as a reduction in sales at the time revenue is recognized and are estimated based on historical experience and contractual obligations. Cabot periodically reviews the assumptions underlying its estimates of discounts and volume rebates and adjusts its revenues accordingly.

Revenue in Purification Solutions is typically recognized when the product is shipped and title and risk of loss have passed to the customer. For major activated carbon injection systems projects, revenue is recognized using the percentage-of-completion method.

Revenue in Advanced Technologies, excluding the Specialty Fluids Business, is typically recognized when the product is shipped and title and risk of loss have passed to the customer. Depending on the nature of the contract with the customer, a portion of the segment's revenue may be recognized using proportional performance. Cabot has technology and licensing agreements with one customer that are accounted for as multiple element arrangements. Revenue is recognized ratably over the term of the agreements, limited by the cumulative amounts that become due, some of which are through 2022.

A significant portion of the revenue in the Specialty Fluids Business, included in Advanced Technologies, arises from the rental of cesium formate. This revenue is recognized throughout the rental period based on the contracted rental terms. Customers are also billed and revenue is recognized, typically at the end of the job, for cesium formate product that is not returned. The Company also generates revenue from cesium formate sold outside of a rental process and revenue is recognized upon delivery of the fluid.

Cabot maintains allowances for doubtful accounts based on an assessment of the collectability of specific customer accounts, the aging of accounts receivable and other economic information on both a historical and prospective basis. Customer account balances are charged against the allowance when it is probable the receivable will not be recovered. There is no off-balance sheet credit exposure related to customer receivable balances.

Property, Plant and Equipment

Property, plant and equipment are recorded at cost. Depreciation of property, plant and equipment is calculated using the straight-line method over the estimated useful lives. The depreciable lives for buildings, machinery and equipment, and other fixed assets are twenty to twenty-five years, ten to twenty-five years, and three to twenty-five years, respectively. The cost and accumulated depreciation for property, plant and equipment sold, retired, or otherwise disposed of are removed from the Consolidated Balance Sheets and resulting gains or losses are included in earnings in the Consolidated Statements of Operations. Expenditures for repairs and maintenance are charged to expenses as incurred. Expenditures for major renewals and betterments, which significantly extend the useful lives of existing plant and equipment, are capitalized and depreciated.

Intangible Assets and Goodwill

The Company records tangible and intangible assets acquired and liabilities assumed in business combinations under the acquisition method of accounting. Amounts paid for an acquisition are allocated to the assets acquired and liabilities assumed based on their fair values at the date of acquisition. Goodwill is comprised of the purchase price of business acquisitions in excess of the fair value assigned to the net tangible and identifiable intangible assets acquired. Goodwill is not amortized but is reviewed for impairment annually, as of May 31, or when events or changes in the business environment indicate that the carrying value of the reporting unit may exceed its fair value. A reporting unit, for the purpose of the impairment test, is at or below the operating segment level, and constitutes a business for which discrete financial information is available and regularly reviewed by segment management. The separate businesses included within Performance Materials are considered separate reporting units. The goodwill balance relative to this segment is recorded in the Fumed Metal Oxides reporting unit within Performance Materials.

For the purpose of the goodwill impairment test, the Company first assesses qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying value amount and as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. Alternatively, the Company may elect to proceed directly to the two-step

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

goodwill impairment test. If an initial qualitative assessment identifies that it is more likely than not that the carrying value of a reporting unit exceeds its estimated fair value, an additional quantitative evaluation is performed under the two-step impairment test. If based on the quantitative evaluation the fair value of the reporting unit is less than its carrying amount, the Company performs an analysis of the fair value of all assets and liabilities of the reporting unit. If the implied fair value of the reporting unit's goodwill is determined to be less than its carrying amount, an impairment is recognized for the difference. The fair value of a reporting unit is based on discounted estimated future cash flows. The assumptions used to estimate fair value include management's best estimates of future growth rates, operating cash flows, capital expenditures, and discount rates over an estimate of the remaining operating period at the reporting unit level. Should the fair value of any of the Company's reporting units decline because of reduced operating performance, market declines, or other indicators of impairment, or as a result of changes in the discount rate, charges for impairment may be necessary. Based on the Company's most recent annual goodwill impairment test the fair values of all of its reporting units were substantially in excess of their carrying values. The Company notes that the future growth in the Purification Solutions business, which had \$469 million of goodwill at March 31, 2014, is highly dependent on the growth in the mercury removal portion of this business. This growth relies upon achieving the expected volumes and margins in the mercury removal portion of this business and significantly depends on the adoption and enforcement of environmental laws and regulations, particularly those that would require U.S. based coal fired electrical utilities to reduce the quantity of air pollutants they release, including mercury, to comply with the Mercury and Air Toxics Standards that become effective in April 2015.

The Company uses assumptions and estimates in determining the fair value of assets acquired and liabilities assumed in a business combination. The determination of the fair value of intangible assets requires the use of significant judgment with regard to (i) assumptions used in the valuation model; and (ii) determination of the intangible assets' useful lives. The Company estimates the fair value of identifiable acquisition-related intangible assets principally based on projections of cash flows that will arise from these assets. The projected cash flows are discounted to determine the fair value of the assets at the dates of acquisition. The Company reviews definite-lived intangible assets for impairment when indication of potential impairment exists, such as a significant reduction in cash flows associated with the assets. Actual cash flows arising from a particular intangible asset could vary from projected cash flows which could imply different carrying values from those established at the dates of acquisition and which could result in impairment of such asset.

The Company evaluates indefinite-lived intangible assets for impairment annually or when events occur or circumstances change that may reduce the fair value of the asset below its carrying amount. The annual review is performed as of May 31. The Company may first perform a qualitative assessment to determine whether it is necessary to perform the quantitative impairment test or bypass the qualitative assessment and proceed directly to performing the quantitative impairment test. The quantitative impairment test is based on discounted estimated future cash flows. The assumptions used to estimate fair value include management's best estimates of future growth rates and discount rates over an estimate of the remaining operating period at the unit of accounting level. The Company's intangible assets are primarily comprised of trademarks, customer relationships, patented and unpatented technology and other intellectual property. Finite lived intangible assets are amortized over their estimated useful lives.

Long-lived Assets

The Company's long-lived assets primarily include property, plant and equipment, long-term investments and assets held for rent. The carrying values of long-lived assets are reviewed for impairment whenever events or changes in business circumstances indicate that the carrying amount of an asset may not be recoverable. An asset impairment is recognized when the carrying value of the asset is not recoverable based on the probability-weighted undiscounted estimated future cash flows to be generated by the asset. The Company's estimates reflect management's assumptions about selling prices, production and sales volumes, costs and market conditions over an estimate of the remaining operating period. If an impairment is indicated, the asset is written down to fair value. If the asset does not have a readily determinable market value, a discounted cash flow model may be used to determine the fair value of the asset. The key inputs to the discounted cash flow would be the same as the undiscounted cash flow noted above, with the addition of the discount rate used. In circumstances when an asset does not have separate identifiable cash flows, an impairment charge is recorded when the Company no longer intends to use the asset.

To test for impairment of assets the Company generally uses a probability-weighted estimate of the future undiscounted net cash flows of the assets over their remaining lives to determine if the value of the asset is recoverable. Long-lived assets are grouped with other assets and liabilities at the lowest level for which independent identifiable cash flows are determinable.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

Income Tax in Interim Periods

The Company records its tax provision or benefit on an interim basis using an estimated annual effective tax rate. This rate is applied to the current period ordinary income or loss to determine the income tax provision or benefit allocated to the interim period. Losses from jurisdictions for which no benefit can be recognized and the income tax effects of unusual or infrequent items are excluded from the estimated annual effective tax rate and are recognized in the impacted interim period.

Valuation allowances are provided against the future tax benefits that arise from the deferred tax assets in jurisdictions for which no benefit can be recognized. The estimated annual effective tax rate may be significantly impacted by nondeductible expenses and the Company's projected earnings mix by tax jurisdiction. Adjustments to the estimated annual effective income tax rate are recognized in the period when such estimates are revised.

Inventory Valuation

Inventories are stated at the lower of cost or market. The cost of all carbon black inventories in the U.S. is determined using the last-in, first-out ("LIFO") method. Had the Company used the first-in, first-out ("FIFO") method instead of the LIFO method for such inventories, the value of those inventories would have been \$54 million and \$55 million higher as of March 31, 2014 and September 30, 2013, respectively. The cost of Specialty Fluids inventories is determined using the average cost method. The cost of other U.S. and non-U.S. inventories is determined using the FIFO method.

Cabot reviews inventory for both potential obsolescence and potential declines in anticipated selling prices. In this review, the Company makes assumptions about the future demand for and market value of the inventory, and based on these assumptions estimates the amount of any obsolete, unmarketable, slow moving or overvalued inventory. Cabot writes down the value of these inventories by an amount equal to the difference between the cost of the inventory and its estimated market value.

Pensions and Other Postretirement Benefits

The Company recognizes the funded status of defined benefit pension and other postretirement benefit plans as an asset or liability. This amount is defined as the difference between the fair value of plan assets and the benefit obligation. The Company is required to recognize as a component of other comprehensive income, net of tax, the actuarial gains/losses and prior service costs/credits that arise but were not previously required to be recognized as components of net periodic benefit cost. Other comprehensive income is adjusted as these amounts are later recognized in income as components of net periodic benefit cost.

Accumulated Other Comprehensive Income

Accumulated other comprehensive income ("AOCI"), which is included as a component of stockholders' equity, includes unrealized gains or losses on available-for-sale marketable securities, currency translation adjustments in foreign subsidiaries, translation adjustments on foreign equity securities and pension liability adjustments.

At the beginning of fiscal 2014, the Company adopted new accounting guidance for the presentation of amounts reclassified from AOCI. The guidance specifically requires, either on the face of the financial statements or in the notes, presentation of significant amounts reclassified from AOCI to net income for each component of AOCI and the respective line items within the Consolidated Statements of Operations. These disclosures are included in Note H to the consolidated financial statements.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

Accumulated other comprehensive items in the accompanying Consolidated Balance Sheets consist of the following items net of tax:

| | <u>March 31,</u> <u>2014</u> | <u>September 30,</u> <u>2013</u> |
|--|---------------------------------|-------------------------------------|
| | (Dollars in millions) | |
| Foreign currency translation adjustments at beginning of period | \$ 154 | \$ 167 |
| Net foreign currency translation adjustments during the period | (27) | (13) |
| Balance at end of period | 127 | 154 |
| Unrealized gain on investments at beginning of period | 2 | — |
| Net unrealized gains during the period | — | 2 |
| Balance at end of period | 2 | 2 |
| Pension and other postretirement benefit plans at beginning of period | (53) | (75) |
| Net change in pension and other postretirement benefit plans during the period | 1 | 22 |
| Balance at end of period | (52) | (53) |
| Total accumulated other comprehensive income | <u>\$ 77</u> | <u>\$ 103</u> |

Recent Accounting Pronouncements

In July 2013, the FASB issued a new standard related to the "Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists". The standard requires, unless certain conditions exist, an unrecognized tax benefit or a portion of an unrecognized tax benefit be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, similar to a tax loss or a tax credit carryforward. This standard is applicable for fiscal years beginning after December 15, 2013, and for interim periods within those years. Accordingly, the Company will adopt this standard beginning October 1, 2014, the beginning of the first quarter of its 2015 fiscal year. The Company is currently evaluating the impact of the adoption of this standard on its consolidated financial statements and it does not expect the impact to be material.

In April 2014, the FASB issued a new standard related to the "Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity". The standard requires discontinued operations treatment for disposals of a component or group of components that represents a strategic shift that has or will have a major impact on an entity's operations or financial results and requires additional disclosures for discontinued operations and new disclosures for individually material disposal transactions that do not meet the definition of a discontinued operation. This standard is applicable for fiscal years beginning after December 15, 2014 and for interim periods within those years with early adoption permitted but only for disposals that have not been reported in financial statements previously issued. Accordingly, the Company expects to adopt this standard beginning October 1, 2015, the beginning of the first quarter of its 2016 fiscal year. The impact of the adoption of this standard may have a material impact on the Company's consolidated financial statements based on the nature of the future disposals.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

C. Acquisition of NHUMO

In November 2013, the Company purchased all of KUO's common stock in the NHUMO joint venture, which represented approximately 60% of the outstanding common stock of the joint venture. Prior to this transaction, the Company owned approximately 40% of the outstanding common stock of NHUMO, and the NHUMO entity was accounted for as an equity affiliate of the Company.

At the close of the transaction, the Company paid KUO \$80 million in cash and NHUMO issued redeemable preferred stock to KUO with a redemption value of \$25 million. The preliminary purchase price was subject to a working capital adjustment calculation, which was finalized during the second quarter of fiscal 2014, and there were no adjustments. The preferred stock will accumulate dividends at a fixed rate of 6% annually and will be redeemable at the option of KUO or the Company for \$25 million starting on the fifth anniversary of the acquisition date or upon the occurrence of certain other conditions. Annual payment by NHUMO of the dividends will be contingent on NHUMO achieving a minimum EBITDA (earnings before interest, taxes, depreciation, and amortization) level and if such minimum EBITDA is not achieved in any year, the dividend will be accumulated and paid at the time the preferred shares are redeemed. The preferred stock issued in connection with the transaction is not mandatorily redeemable and has embedded put and call rights at the fixed redemption price. Accordingly, the instrument is accounted for as a financing obligation and has been separately presented in the Consolidated Balance Sheets as a long term liability. Upon acquisition, the Company began consolidating NHUMO into its consolidated financial statements. Prior to closing, the Company received a \$14 million dividend from NHUMO.

The Company incurred acquisition costs of approximately \$1 million through March 31, 2014 associated with the transaction, which are included in Selling and administrative expenses in the Consolidated Statements of Operations.

The allocation of the purchase price set forth below was based on preliminary estimates of the fair value of assets acquired, liabilities assumed, and Cabot's previously held equity interest in NHUMO as of the acquisition date. The Company is continuing to obtain information to complete its valuation of these accounts and the associated tax accounting.

| | (in millions) |
|--|----------------------|
| Assets | |
| Cash | \$ 7 |
| Accounts receivable | 33 |
| Inventories | 14 |
| Property, plant and equipment | 48 |
| Other non-current assets | 1 |
| Intangible assets | 57 |
| Goodwill | 51 |
| Total assets acquired | <u>211</u> |
| Liabilities | |
| Current liabilities | (18) |
| Deferred tax liabilities | (31) |
| Total liabilities assumed | <u>(49)</u> |
| Net assets acquired | \$ 162 |
| Cash consideration paid | 80 |
| Fair value of redeemable preferred stock | 28 |
| Previously held equity interest in NHUMO | 54 |
| Total | <u>\$ 162</u> |

As a result of the acquisition, the Company recorded a gain of \$29 million for the difference between the carrying value and the fair value of the previously held equity interest in NHUMO, which was included in Other (expense) income. The fair value of \$54 million for the previously held equity interest was determined based on the fair value of Cabot's pre-existing interest in NHUMO as adjusted for a control premium derived from synergies gained as a result of the Company obtaining control of NHUMO.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

As part of the preliminary purchase price allocation, the Company determined that a separately identifiable intangible asset was customer relationships in the amount of \$57 million, which is being amortized over a period of 17 years. The Company estimated the fair value of the identifiable acquisition-related intangible asset based on projections of cash flows that will arise from the asset. The projected cash flows are discounted to determine the fair value of the asset at the date of acquisition. The determination of the fair value of the intangible asset acquired required the use of significant judgment with regard to (i) assumptions in the discounted cash flow model used and (ii) determination of the useful life of customer relationships.

The fair value of the redeemable preferred stock was determined based on a discounted cash flow model, using the expected timing of the cash flows and an appropriate discount rate.

The excess of the preliminary purchase price over the fair value of the tangible net assets and intangible asset acquired, the issuance of redeemable preferred stock and the previously held equity interest in NHUMO was recorded as goodwill. The goodwill recognized is attributable to the expected growth and operating synergies that the Company expects to realize from this acquisition. Goodwill generated from the acquisition will not be deductible for tax purposes.

D. Discontinued Operations and Notes Receivable from Sale of Business

In January 2012, the Company sold its Supermetals Business to Global Advanced Metals Pty Ltd., an Australian company ("GAM"), for \$452 million, including cash consideration of \$175 million received on the closing date and notes receivable ("GAM Notes") totaling \$277 million payable at various dates through March 2014. The carrying value of the GAM Notes at March 31, 2014 was \$215 million, which was presented as Notes receivable from sale of business on the Consolidated Balance Sheets. In the first week of April 2014, Cabot received the final payment on the GAM Notes in the amount of \$215 million.

In March 2014, the Company entered into an agreement to sell its Security Materials business to SICPA, for approximately \$20 million in cash. The sale is expected to close by the end of fiscal year 2014, pending regulatory approvals. The business is being accounted for as discontinued operations, and the applicable assets of the business have been classified as held for sale in the Consolidated Balance Sheets as of March 31, 2014 and September 30, 2013. The Consolidated Statements of Operations for all periods presented have been recast to reflect the Security Materials business in discontinued operations. Unless otherwise indicated, all disclosures and amounts in the Notes to Consolidated Financial Statements relate to the Company's continuing operations. The Company's Consolidated Statements of Cash Flows include the cash flows from both continuing and discontinued operations.

The following table summarizes the results from discontinued operations during the three and six months ended March 31, 2014 and 2013:

| | <u>Three Months Ended</u> | | <u>Six Months Ended</u> | |
|---|---------------------------|---------------|-------------------------|---------------|
| | <u>March 31</u> | | <u>March 31</u> | |
| | <u>2014</u> | <u>2013</u> | <u>2014</u> | <u>2013</u> |
| | (Dollars in millions) | | | |
| Net sales and other operating revenues | \$ 2 | \$ 2 | \$ 3 | \$ 3 |
| Loss from operations before income taxes | (1) | (1) | (2) | (5) |
| Benefit from income taxes | 1 | — | 1 | 2 |
| Loss from discontinued operations, net of tax | <u>\$ —</u> | <u>\$ (1)</u> | <u>\$ (1)</u> | <u>\$ (3)</u> |

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

The following table summarizes the assets held for sale in the Company's Consolidated Balance Sheets:

| | March 31, 2014 | September 30, 2013 |
|---------------------------------------|----------------|--------------------|
| (Dollars in millions) | | |
| Assets | | |
| Inventories | 3 | 3 |
| Total current assets held for sale | <u>\$ 3</u> | <u>\$ 3</u> |
| Property, plant and equipment, net | 4 | 5 |
| Goodwill | 2 | 2 |
| Intangible assets, net | 2 | 2 |
| Total noncurrent assets held for sale | <u>\$ 8</u> | <u>\$ 9</u> |

E. Employee Benefit Plans

Net periodic defined benefit pension and other postretirement benefit costs include the following:

| | Three Months Ended March 31 | | | | | | | |
|--------------------------------------|-----------------------------|-------------|-------------|-------------|-------------------------|-------------|---------------|-------------|
| | 2014 | | | | 2013 | | | |
| | Pension Benefits | | | | Postretirement Benefits | | | |
| | U.S. | Foreign | U.S. | Foreign | U.S. | Foreign | U.S. | Foreign |
| | (Dollars in millions) | | | | | | | |
| Service cost | \$— | \$ 3 | \$ 2 | \$ 3 | \$— | \$ — | \$— | \$ — |
| Interest cost | 2 | 4 | 1 | 3 | — | — | — | — |
| Expected return on plan assets | (2) | (5) | (2) | (4) | — | — | — | — |
| Amortization of prior service credit | — | — | — | — | — | — | (1) | — |
| Amortization of actuarial loss | — | 1 | — | 1 | — | — | — | — |
| Net periodic benefit cost | <u>\$—</u> | <u>\$ 3</u> | <u>\$ 1</u> | <u>\$ 3</u> | <u>\$—</u> | <u>\$ —</u> | <u>\$ (1)</u> | <u>\$ —</u> |

| | Six Months Ended March 31 | | | | | | | |
|--------------------------------------|---------------------------|-------------|-------------|-------------|-------------------------|-------------|---------------|-------------|
| | 2014 | | | | 2013 | | | |
| | Pension Benefits | | | | Postretirement Benefits | | | |
| | U.S. | Foreign | U.S. | Foreign | U.S. | Foreign | U.S. | Foreign |
| | (Dollars in millions) | | | | | | | |
| Service cost | \$ 1 | \$ 5 | \$ 3 | \$ 5 | \$— | \$ — | \$— | \$ — |
| Interest cost | 4 | 8 | 3 | 7 | 1 | — | 1 | — |
| Expected return on plan assets | (5) | (10) | (5) | (9) | — | — | — | — |
| Amortization of prior service credit | — | — | — | — | (1) | — | (2) | — |
| Amortization of actuarial loss | — | 2 | 1 | 2 | — | — | — | — |
| Net periodic benefit cost | <u>\$—</u> | <u>\$ 5</u> | <u>\$ 2</u> | <u>\$ 5</u> | <u>\$—</u> | <u>\$ —</u> | <u>\$ (1)</u> | <u>\$ —</u> |

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

F. Goodwill and Other Intangible Assets

Cabot had goodwill balances of \$555 million and \$502 million at March 31, 2014 and September 30, 2013, respectively. Goodwill of \$2 million which was presented under the Advanced Technologies reportable segment as of September 30, 2013 has been reclassified to Assets held for sale in the Company's Consolidated Balance Sheets for all periods presented as a result of the pending divestiture of the Security Materials business discussed in Note D. The carrying amount of goodwill attributable to each reportable segment with goodwill balances and the changes in those balances during the period ended March 31, 2014 are as follows:

| | Reinforcement Materials | Performance Materials | Purification Solutions | Total |
|-------------------------------|----------------------------|--------------------------|---------------------------|--------------|
| | (Dollars in millions) | | | |
| Balance at September 30, 2013 | \$ 25 | \$ 11 | \$ 466 | \$502 |
| Goodwill acquired(1) | 51 | — | — | 51 |
| Foreign currency impact | (1) | — | 3 | 2 |
| Balance at March 31, 2014 | <u>\$ 75</u> | <u>\$ 11</u> | <u>\$ 469</u> | <u>\$555</u> |

(1) Goodwill acquired relates to the NHUMO transaction as described in Note C.

Goodwill impairment tests are performed at least annually. The Company performed its last annual impairment assessment as of May 31, 2013 and determined there was no impairment.

Net intangible assets of \$2 million which were presented as other intangible assets as of September 30, 2013 have been reclassified to Assets held for sale in the Company's Consolidated Balance Sheets for all periods presented as a result of the pending divestiture of the Security Materials business discussed in Note D. The following table provides information regarding the Company's intangible assets:

| | March 31, 2014 | | | September 30, 2013 | | |
|--|----------------------------|-----------------------------|-----------------------------|----------------------------|-----------------------------|-----------------------------|
| | Gross Carrying Value | Accumulated Amortization | Net Intangible Assets | Gross Carrying Value | Accumulated Amortization | Net Intangible Assets |
| | (Dollars in millions) | | | | | |
| Intangible assets with finite lives | | | | | | |
| Developed technology | \$ 156 | \$ (13) | \$ 143 | \$ 154 | \$ (9) | \$ 145 |
| Customer relationships(1) | 170 | (12) | 158 | 113 | (7) | 106 |
| Total intangible assets, finite lives | <u>\$ 326</u> | <u>\$ (25)</u> | <u>\$ 301</u> | <u>\$ 267</u> | <u>\$ (16)</u> | <u>\$ 251</u> |
| Trademarks, indefinite lives | 57 | — | 57 | 57 | — | 57 |
| Total intangible assets | <u>\$ 383</u> | <u>\$ (25)</u> | <u>\$ 358</u> | <u>\$ 324</u> | <u>\$ (16)</u> | <u>\$ 308</u> |

(1) The change in the gross carrying value of the Customer relationships intangible asset is primarily due to the NHUMO transaction as described in Note C.

Intangible assets with finite lives are amortized over their estimated useful lives, which range from six to twenty years, with a weighted average amortization period of approximately 19 years. Amortization expense for the three months ended March 31, 2014 and 2013 was \$5 million and \$3 million, respectively, and is included in Cost of sales and Selling and administrative expenses in the Consolidated Statements of Operations. Amortization expense for the six months ended March 31, 2014 and 2013 was \$9 million and \$6 million, respectively, and is included in Cost of sales and Selling and administrative expenses in the Consolidated Statements of Operations. Total amortization expense is estimated to be approximately \$18 million each year for the next five fiscal years. Intangible assets with indefinite lives are evaluated for impairment at least annually. The Company performed its last annual impairment assessment as of May 31, 2013, and determined there was no impairment.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

G. Stockholders' Equity

In fiscal 2007, the Board of Directors authorized Cabot to repurchase up to ten million shares of Cabot's common stock in the open market or in privately negotiated transactions. This authorization does not have a set expiration date. During the first six months of both fiscal 2014 and 2013, Cabot repurchased 379 shares of its common stock under this authorization. As of March 31, 2014, approximately 1.6 million shares remain available for repurchase under the current authorization.

During the six months ended March 31 of both fiscal 2014 and 2013, Cabot paid cash dividends to common stockholders of \$26 million in the aggregate.

Noncontrolling interests

The following table illustrates the noncontrolling interests activity for the periods presented:

| | 2014 | 2013 |
|---|-----------------------|---------------|
| | (Dollars in millions) | |
| Balance at September 30 | \$ 132 | \$ 126 |
| Net income attributable to noncontrolling interests | 9 | — |
| Noncontrolling interest foreign currency translation adjustment | (2) | — |
| Contribution from noncontrolling interests | — | 9 |
| Noncontrolling interest dividends | (20) | (13) |
| Balance at March 31 | <u>\$ 119</u> | <u>\$ 122</u> |

H. Accumulated Other Comprehensive Income

Comprehensive income combines net income and other comprehensive income items, which are reported as components of stockholders' equity in the accompanying Consolidated Balance Sheets.

Changes in each component of Accumulated other comprehensive income, net of tax, are as follows:

| | Currency Translation Adjustment | Unrealized Gains on Investments | Pension and Other Postretirement Benefit Liability Adjustments | Total |
|--|---------------------------------------|---------------------------------------|---|--------------|
| | (Dollars in millions) | | | |
| Balance at September 30, 2013, attributable to Cabot Corporation | \$ 154 | \$ 2 | \$ (53) | \$103 |
| Other comprehensive loss before reclassifications | (29) | — | — | (29) |
| Amounts reclassified from accumulated other comprehensive income | — | — | 1 | 1 |
| Net other comprehensive items | (29) | — | 1 | (28) |
| Balance at March 31, 2014 | <u>125</u> | <u>2</u> | <u>(52)</u> | <u>75</u> |
| Less: Noncontrolling interest | (2) | — | — | (2) |
| Balance at March 31, 2014, attributable to Cabot Corporation | <u>\$ 127</u> | <u>\$ 2</u> | <u>\$ (52)</u> | <u>\$ 77</u> |

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

The amounts reclassified out of Accumulated other comprehensive income and into the Statement of Operations for the six months ended March 31, 2014 and 2013 are as follows:

| | <u>Affected Line Item in the Consolidated Statements of Operations</u> | <u>Six Months Ended March 31,</u> | |
|--|--|-----------------------------------|-------------|
| | | <u>2014</u> | <u>2013</u> |
| (Dollars in millions) | | | |
| Pension and other postretirement benefit liability adjustment | | | |
| Amortization of actuarial losses | Net Periodic Benefit Cost - see Note E for details | \$ 2 | \$ 3 |
| Amortization of prior service cost | Net Periodic Benefit Cost - see Note E for details | (1) | (2) |
| Total before tax | | 1 | 1 |
| Tax impact | Provision for income taxes | — | — |
| Total after tax | | <u>\$ 1</u> | <u>\$ 1</u> |

I. Commitments and Contingencies

Purchase Commitments

Cabot has entered into long-term purchase agreements primarily for the purchase of raw materials. Under certain of these agreements the quantity of material being purchased is fixed, but the price paid changes as market prices change. For those commitments, the amounts included in the table below are based on market prices at March 31, 2014.

| | <u>Payments Due by Fiscal Year</u> | | | | | | <u>Total</u> |
|-------------------------|-------------------------------------|--------------|--------------|--------------|--------------|-------------------|----------------|
| | <u>Remainder of Fiscal 2014</u> | <u>2015</u> | <u>2016</u> | <u>2017</u> | <u>2018</u> | <u>Thereafter</u> | |
| (Dollars in millions) | | | | | | | |
| Reinforcement Materials | \$ 202 | \$321 | \$300 | \$186 | \$178 | \$ 2,795 | \$3,982 |
| Performance Materials | 23 | 39 | 33 | 30 | 30 | 236 | 391 |
| Advanced Technologies | 1 | 2 | 1 | 1 | 1 | — | 6 |
| Purification Solutions | 15 | 16 | 9 | 9 | 9 | 16 | 74 |
| Total | <u>\$ 241</u> | <u>\$378</u> | <u>\$343</u> | <u>\$226</u> | <u>\$218</u> | <u>\$ 3,047</u> | <u>\$4,453</u> |

Guarantee Agreements

Cabot has provided certain indemnities pursuant to which it may be required to make payments to an indemnified party in connection with certain transactions and agreements. In connection with certain acquisitions and divestitures, Cabot has provided routine indemnities with respect to such matters as environmental, tax, insurance, product and employee liabilities. In connection with various other agreements, including service and supply agreements, Cabot may provide routine indemnities for certain contingencies and routine warranties. Cabot is unable to estimate the maximum potential liability for these types of indemnities as a maximum obligation is not explicitly stated in most cases and the amounts, if any, are dependent upon the outcome of future contingent events, the nature and likelihood of which cannot be reasonably estimated. The durations of the indemnities vary, and in many cases are indefinite. Cabot has not recorded any liability for these indemnities in the consolidated financial statements, except as otherwise disclosed.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

Contingencies

Cabot is a defendant, or potentially responsible party, in various lawsuits and environmental proceedings wherein substantial amounts are claimed or at issue.

Environmental Matters

As of March 31, 2014 and September 30, 2013, Cabot had \$17 million and \$5 million, respectively, reserved for environmental matters, substantially all of which is accounted for on an undiscounted basis. These matters mainly relate to closed sites. During the three months ended March 31, 2014, additional information related to required environmental actions became available, resulting in the recognition of a \$13 million liability as the cost of these actions became probable and estimable. These reserves represent Cabot's best estimates of the probable costs likely to be incurred at those sites where costs are reasonably estimable based on its analysis of the extent of clean up required, alternative clean-up methods available, abilities of other responsible parties to contribute and its interpretation of laws and regulations applicable to each site. Cash payments related to these environmental matters were \$1 million in the first six months of both fiscal 2014 and 2013. Cabot reviews the adequacy of the reserves as circumstances change at individual sites and adjusts the reserves as appropriate. Almost all of Cabot's reserves relate to environmental issues that are mature and have been investigated and studied and, in many cases, are subject to agreed upon remediation plans. However, depending on the results of future testing, changes in risk assessment practices, remediation techniques and regulatory requirements, newly discovered conditions, and other factors, it is reasonably possible that the Company could incur additional costs in excess of environmental reserves currently recorded. Management estimates, based on the latest available information, that any such future environmental remediation costs that are reasonably possible to be in excess of amounts already recorded would be immaterial to the Company's consolidated financial statements.

Other Matters

Respirator Liabilities

Cabot has exposure in connection with a safety respiratory products business that a subsidiary acquired from American Optical Corporation ("AO") in an April 1990 asset purchase transaction. The subsidiary manufactured respirators under the AO brand and disposed of that business in July 1995. In connection with its acquisition of the business, the subsidiary agreed, in certain circumstances, to assume a portion of AO's liabilities, including costs of legal fees together with amounts paid in settlements and judgments, allocable to AO respiratory products used prior to the 1990 purchase by the Cabot subsidiary. As more fully described in Cabot's 2013 10-K, the respirator liabilities involve claims for personal injury, including asbestosis, silicosis and coal worker's pneumoconiosis, allegedly resulting from the use of respirators that are alleged to have been negligently designed or labeled.

As of March 31, 2014 and September 30, 2013, there were approximately 41,000 and 42,000 claimants, respectively, in pending cases asserting claims against AO in connection with respiratory products. Cabot has a reserve to cover its expected share of liability for existing and future respirator liability claims. At March 31, 2014 and September 30, 2013, the reserve was \$9 million and \$11 million, respectively, on a discounted basis (\$13 million and \$15 million on an undiscounted basis at March 31, 2014 and September 30, 2013, respectively). The reserve is being accreted up to the undiscounted liability through interest expense over the expected cash flow period, which is through 2065. Cash payments related to this liability were \$2 million and \$1 million in the first six months of fiscal 2014 and 2013, respectively.

Other

The Company is subject to various other lawsuits, claims and contingent liabilities arising in the ordinary course of its business and with respect to the Company's divested businesses. In the opinion of the Company, although final disposition of some or all of these other suits and claims may impact the Company's consolidated financial statements in a particular period, they should not, in the aggregate, have a material adverse effect on the Company's financial position.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

J. Income Tax Uncertainties

Cabot files U.S. federal and state and non-U.S. income tax returns in jurisdictions with varying statutes of limitations. The 2007 through 2013 tax years remain subject to examination by the IRS and various tax years from 2005 through 2013 remain subject to examination by the respective state tax authorities. In significant non-U.S. jurisdictions, various tax years from 2001 through 2013 remain subject to examination by their respective tax authorities. Cabot's significant non-U.S. jurisdictions include Canada, China, France, Germany, Italy, Japan, and the Netherlands.

Certain Cabot subsidiaries are under audit in jurisdictions outside of the U.S. In addition, certain statutes of limitations are scheduled to expire in the near future. It is reasonably possible that a change in the unrecognized tax benefits may also occur within the next twelve months related to the settlement of one or more of these audits, however, an estimated range of the impact on the unrecognized tax benefits cannot be quantified at this time.

During the three months ended March 31, 2014, Cabot reached a bilateral agreement with the tax authorities in the U.S. and Canada that covered the fiscal years 2001 through 2012, resulting in a \$6 million net benefit. In addition, Cabot expects to recover prepaid taxes of approximately \$16 million from the Canadian government during fiscal 2014.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

K. Earnings Per Share

The following tables summarize the components of the basic and diluted earnings per common share computations:

| | <u>Three Months Ended</u> <u>March 31</u> | | <u>Six Months Ended</u> <u>March 31</u> | |
|---|--|----------------|--|----------------|
| | <u>2014</u> | <u>2013</u> | <u>2014</u> | <u>2013</u> |
| (Dollars and shares in millions, except per share amounts) | | | | |
| Basic EPS: | | | | |
| Net income attributable to Cabot Corporation | \$ 36 | \$ 27 | \$ 116 | \$ 47 |
| Less: Dividends and dividend equivalents to participating securities | — | — | — | — |
| Less: Undistributed earnings allocated to participating securities (1) | — | — | 1 | — |
| Earnings allocated to common shareholders (numerator) | <u>\$ 36</u> | <u>\$ 27</u> | <u>\$ 115</u> | <u>\$ 47</u> |
| | | | | |
| Weighted average common shares and participating securities outstanding | 65.0 | 64.3 | 64.8 | 64.2 |
| Less: Participating securities(1) | 0.6 | 0.6 | 0.6 | 0.6 |
| Adjusted weighted average common shares (denominator) | <u>64.4</u> | <u>63.7</u> | <u>64.2</u> | <u>63.6</u> |
| | | | | |
| Amounts per share - basic: | | | | |
| Income from continuing operations attributable to Cabot Corporation | \$ 0.56 | \$ 0.44 | \$ 1.81 | \$ 0.79 |
| Loss from discontinued operations | (0.01) | (0.01) | (0.02) | (0.05) |
| Net income attributable to Cabot Corporation | <u>\$ 0.55</u> | <u>\$ 0.43</u> | <u>\$ 1.79</u> | <u>\$ 0.74</u> |
| Diluted EPS: | | | | |
| Earnings allocated to common shareholders | \$ 36 | \$ 27 | \$ 115 | \$ 47 |
| Plus: Earnings allocated to participating securities | — | — | 1 | — |
| Less: Adjusted earnings allocated to participating securities (2) | — | — | (1) | — |
| Earnings allocated to common shareholders (numerator) | <u>\$ 36</u> | <u>\$ 27</u> | <u>\$ 115</u> | <u>\$ 47</u> |
| | | | | |
| Adjusted weighted average common shares outstanding | 64.4 | 63.7 | 64.2 | 63.6 |
| Effect of dilutive securities: | | | | |
| Common shares issuable(3) | 0.7 | 0.7 | 0.8 | 0.7 |
| Adjusted weighted average common shares (denominator) | <u>65.1</u> | <u>64.4</u> | <u>65.0</u> | <u>64.3</u> |
| | | | | |
| Amounts per share - diluted: | | | | |
| Income from continuing operations attributable to Cabot Corporation | \$ 0.55 | \$ 0.43 | \$ 1.79 | \$ 0.78 |
| Loss from discontinued operations | (0.01) | (0.01) | (0.02) | (0.05) |
| Net income attributable to Cabot Corporation | <u>\$ 0.54</u> | <u>\$ 0.42</u> | <u>\$ 1.77</u> | <u>\$ 0.73</u> |

(1) Participating securities consist of shares of unvested restricted stock and unvested time-based restricted stock units.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

Undistributed earnings are the earnings which remain after dividends declared during the period are assumed to be distributed to the common and participating shareholders. Undistributed earnings are allocated to common and participating shareholders on the same basis as dividend distributions. The calculation of undistributed earnings is as follows:

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|--|--------------------------------|--------------|------------------------------|--------------|
| | 2014 | 2013 | 2014 | 2013 |
| (Dollars in millions) | | | | |
| Calculation of undistributed earnings: | | | | |
| Net income attributable to Cabot Corporation | \$ 36 | \$ 27 | \$ 116 | \$ 47 |
| Less: Dividends declared on common stock | 13 | 13 | 26 | 26 |
| Less: Dividends declared on participating securities | — | — | — | — |
| Undistributed earnings | <u>\$ 23</u> | <u>\$ 14</u> | <u>\$ 90</u> | <u>\$ 21</u> |
| Allocation of undistributed earnings: | | | | |
| Undistributed earnings allocated to common shareholders | \$ 23 | \$ 14 | \$ 89 | \$ 21 |
| Undistributed earnings allocated to participating shareholders | — | — | 1 | — |
| Undistributed earnings | <u>\$ 23</u> | <u>\$ 14</u> | <u>\$ 90</u> | <u>\$ 21</u> |

- (2) Undistributed earnings are adjusted for the assumed distribution of dividends to the dilutive securities, which are described in (3) below, and then reallocated to participating securities.
- (3) Represents incremental shares of common stock from the (i) assumed exercise of stock options issued under Cabot's equity incentive plans; (ii) assumed issuance of shares to employees pursuant to the Company's Deferred Compensation and Supplemental Retirement Plan; and (iii) assumed issuance of shares under outstanding performance-based restricted stock unit awards issued under Cabot's equity incentive plans. For the three and six months ended March 31, 2014, 203,019 and 220,866 incremental shares of common stock, respectively, were not included in the calculation of diluted earnings per share because the inclusion of these shares would have been antidilutive. For the three and six months ended March 31, 2013, 308,000 and 418,000 incremental shares of common stock, respectively, were not included in the calculation of diluted earnings per share because the inclusion of these shares would have been antidilutive.

L. Restructuring

Cabot's restructuring activities were recorded in the Consolidated Statements of Operations as follows:

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|-------------------------------------|--------------------------------|--------------|------------------------------|--------------|
| | 2014 | 2013 | 2014 | 2013 |
| (Dollars in millions) | | | | |
| Cost of sales | \$ 5 | \$ 18 | \$ 9 | \$ 21 |
| Selling and administrative expenses | 11 | 1 | 12 | 3 |
| Total | <u>\$ 16</u> | <u>\$ 19</u> | <u>\$ 21</u> | <u>\$ 24</u> |

Details of these restructuring activities and the related reserves during the three months ended March 31, 2014 are as follows:

| | Severance and Employee Benefits | Environmental Remediation | Asset Sales | Other | Total |
|------------------------------|---------------------------------------|------------------------------|----------------|-------------|-------------|
| | (Dollars in millions) | | | | |
| Reserve at December 31, 2013 | \$ 4 | \$ 2 | \$— | \$ 2 | \$ 8 |
| Charges | 13 | 1 | 1 | 1 | 16 |
| Cash paid | (1) | (1) | (1) | (1) | (4) |
| Reserve at March 31, 2014 | <u>\$ 16</u> | <u>\$ 2</u> | <u>\$—</u> | <u>\$ 2</u> | <u>\$20</u> |

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

Details of these restructuring activities and the related reserves during the six months ended March 31, 2014 are as follows:

| | Severance and Employee Benefits | Environmental Remediation | Asset Impairment and Accelerated Depreciation | Other | Total |
|--|---------------------------------------|------------------------------|---|-------------|--------------|
| (Dollars in millions) | | | | | |
| Reserve at September 30, 2013 | \$ 7 | \$ 2 | \$ — | \$ 1 | \$ 10 |
| Charges | 14 | 1 | 3 | 3 | 21 |
| Costs charged against assets / liabilities | — | — | (3) | — | (3) |
| Cash paid | (5) | (1) | — | (2) | (8) |
| Reserve at March 31, 2014 | <u>\$ 16</u> | <u>\$ 2</u> | <u>\$ —</u> | <u>\$ 2</u> | <u>\$ 20</u> |

Shared Service Center Transition

In January 2014, the Company announced its intention to open a new Europe, Middle East and Africa (“EMEA”) Shared Service Center in Riga, Latvia, and to close its Leuven, Belgium site, subject to the Belgian information and consultation process. These proposed actions were developed following an extensive evaluation of the Company’s shared service capabilities in the EMEA region and a determination that the proposed future EMEA Shared Service Center will enable the Company to provide the highest quality of service at the most competitive cost.

The Company has recorded \$14 million of pre-tax cash charges during the three months ended March 31, 2014 related to this plan, comprised primarily of employee severance. The Company expects that the majority of actions related to the transition of the shared service center will occur in calendar 2014 and result in total pre-tax cash charges between \$22 million and \$26 million. Through March 31, 2014, the Company has made \$1 million in cash payments related to this plan, mainly related to transition costs, and expects to make cash payments of \$7 million in the second half of fiscal 2014 and the remainder (between \$14 million and \$18 million) in fiscal 2015.

As of March 31, 2014, Cabot has \$13 million of accrued restructuring costs in the Consolidated Balance Sheets related to this closure which is mainly comprised of accrued severance charges.

Closure of Port Dickson, Malaysia Manufacturing Facility

On April 26, 2013, the Company announced that the Board of its joint venture carbon black company, Cabot Malaysia Sdn. Bhd. (“CMSB”), decided to cease carbon black production at its Port Dickson, Malaysia facility. The facility ceased production in June 2013. The Company holds a 51 percent equity share in CMSB. The decision, which affected approximately 90 carbon black employees, was driven by the facility’s manufacturing inefficiencies and raw materials costs.

The Company has recorded pre-tax charges of \$2 million and \$16 million in the six months ended March 31, 2014 and 2013, respectively, related to this closure and \$1 million and \$16 million for the three months ended March 31, 2014 and 2013, respectively. Fiscal 2013 costs were comprised of asset impairment charges whereas fiscal 2014 charges are comprised primarily of site demolition, clearing and environmental remediation.

Through March 31, 2014, the consolidated joint venture has recorded pre-tax restructuring costs of approximately \$20 million comprised mainly of accelerated depreciation and asset write-offs of \$15 million, severance charges of \$2 million, site demolition, clearing and environmental remediation charges of \$2 million, and other closure related charges of \$1 million. CMSB’s net income or loss is attributable to Cabot Corporation and to the noncontrolling interest in the joint venture. The portion of the charges that are allocable to the noncontrolling interest in CMSB (49%) are recorded within Net income (loss) attributable to noncontrolling interests, net of tax, in the Consolidated Statements of Operations.

The Company expects that the majority of actions related to closure of the plant will be completed in fiscal 2014 and result in total pre-tax charges to the consolidated joint venture of approximately \$23 million. The expected charges are comprised of asset impairments and accelerated depreciation of \$15 million, site demolition, clearing and environmental remediation of \$5 million, severance charges of \$2 million, and other closure related charges of \$1 million.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

Cumulative net cash outlays related to this plan are expected to be approximately \$8 million comprised primarily of \$5 million for site demolition, clearing and environmental remediation, \$2 million for severance, and \$1 million for other closure related charges. Through March 31, 2014, CMSB has made approximately \$3 million in cash payments related to this plan related mainly to severance and site demolition and clearing costs.

CMSB expects to make net cash payments of \$5 million during the remainder of fiscal 2014 mainly comprised of site demolition, clearing and environmental remediation costs. These amounts exclude any proceeds that may be received from the sale of land or other manufacturing assets.

As of March 31, 2014, Cabot has \$1 million of accrued restructuring costs in the Consolidated Balance Sheets related to this closure which is mainly comprised of accrued severance charges.

Other Activities

The Company has recorded pre-tax charges of approximately \$4 million and \$6 million during the first six months of fiscal 2014 and fiscal 2013, respectively, and less than \$1 million and \$2 million for the three months ended March 31, 2014 and 2013, respectively, related to restructuring activities at several other locations. Fiscal 2014 charges are comprised mainly of accelerated depreciation and asset write-offs whereas fiscal 2013 costs are comprised mainly of severance-related charges. The Company anticipates recording additional charges of \$2 million during the remainder of fiscal 2014 and thereafter related to these actions.

Through March 31, 2014, Cabot has made cash payments of \$15 million related to these activities and expects to pay \$3 million in the remainder of fiscal 2014 and thereafter mainly for severance and other closure related costs at the impacted locations.

As of March 31, 2014, Cabot has \$1 million of accrued severance and other closure related costs in the Consolidated Balance Sheets related to these activities.

Previous Actions and Sites Pending Sale

Beginning in fiscal 2009, the Company entered into several different restructuring plans which have been substantially completed, pending the sale of former manufacturing sites in Thane, India, Stanlow, U.K. and Hong Kong. The Company has incurred total cumulative pre-tax charges of approximately \$163 million related to these plans as of March 31, 2014 comprised of \$67 million for severance charges, \$65 million for accelerated depreciation and asset impairments, \$10 million for environmental, demolition and site clearing costs, and \$22 million of other closure related charges partially offset by gains on asset sales of \$1 million. These amounts do not include any gain that may be recorded if the Company successfully sells its land rights and certain manufacturing related assets in India and Hong Kong or its land in the U.K.

Pre-tax restructuring expenses related to these plans were approximately \$1 million and \$2 million during the first six months of fiscal 2014 and 2013, respectively, and approximately \$1 million in the three months ended March 31, 2014 and 2013, respectively.

Beginning in fiscal 2009, Cabot has made net cash payments of \$84 million related to these plans and expects to pay an additional \$4 million in the remainder of fiscal 2014 and thereafter. The remaining payments consist mainly of environmental, severance, and other closure related costs. These amounts do not include any proceeds that may be received if the Company successfully sells its land rights and certain manufacturing related assets in India and Hong Kong or its land in the U.K.

As of March 31, 2014, Cabot has \$4 million of accrued environmental, severance, and other closure related costs in the Consolidated Balance Sheets related to these activities.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

M. Financial Instruments and Fair Value Measurements

The FASB authoritative guidance on fair value measurements defines fair value, provides a framework for measuring fair value in generally accepted accounting principles, and requires certain disclosures about fair value measurements. The disclosures focus on the inputs used to measure fair value. The guidance establishes the following hierarchy for categorizing these inputs:

Level 1 — Quoted market prices in active markets for identical assets or liabilities

Level 2 — Significant other observable inputs (e.g., quoted prices for similar items in active markets, quoted prices for identical or similar items in markets that are not active, inputs other than quoted prices that are observable such as interest rate and yield curves, and market-corroborated inputs)

Level 3 — Significant unobservable inputs

There were no transfers of financial assets or liabilities measured at fair value between Level 1 and Level 2, or transfers into or out of Level 3, during the first six months of both fiscal 2014 and 2013.

The GAM Notes as described in Note D are carried at amortized cost and the carrying value was \$215 million at March 31, 2014, which was equivalent to their fair value. The Notes were paid in full in the first week of April 2014.

At March 31, 2014 and September 30, 2013, the fair value of Guaranteed investment contracts, included in Other assets in the Consolidated Balance Sheets, was \$15 million and \$14 million, respectively. Guaranteed investment contracts were classified as Level 2 instruments within the fair value hierarchy as the fair value determination was based on the other observable inputs.

At March 31, 2014 and September 30, 2013, the fair values of cash and cash equivalents, accounts and notes receivable, accounts payable and accrued liabilities, and notes payable approximated their carrying values due to the short-term nature of these instruments. The carrying value of the long-term fixed rate debt was \$958 million and \$971 million, at March 31, 2014 and September 30, 2013, respectively. The fair value of the long-term fixed rate debt was \$1.01 billion at both March 31, 2014 and September 30, 2013. The fair values of Cabot's fixed rate long-term debt are estimated based on comparable quoted market prices at the respective period ends. The carrying amounts of Cabot's floating rate long-term debt and capital lease obligations approximate their fair values. All such measurements are based on observable inputs and are classified as Level 2 within the fair value hierarchy. The valuation technique used is the discounted cash flow model.

N. Derivatives

Interest Rate Risk Management

Cabot's objective is to maintain a certain fixed-to-variable interest rate mix on the Company's debt obligations. Cabot may enter into interest rate swaps as a hedge of the underlying debt instruments to effectively change the characteristics of the interest rate without changing the debt instrument. As of both March 31, 2014 and September 30, 2013, there were no derivatives held to manage interest rate risk.

Foreign Currency Risk Management

Cabot's international operations are subject to certain risks, including currency exchange rate fluctuations and government actions. Cabot endeavors to match the currency in which debt is issued to the currency of the Company's major, stable cash receipts. In some situations Cabot may issue debt denominated in U.S. dollars and enter into cross currency swaps that exchange the dollar principal and interest payments into a currency where the Company expects long-term, stable cash receipts.

Additionally, the Company has foreign currency exposure arising from its net investments in foreign operations. Cabot may enter into cross-currency swaps to mitigate the impact of currency rate changes on the Company's net investments.

The Company also has foreign currency exposure arising from the denomination of assets and liabilities in foreign currencies other than the functional currency of a given subsidiary as well as the risk that currency fluctuations could affect the dollar value of future cash flows generated in foreign currencies. Accordingly, Cabot uses forward contracts to minimize the exposure to foreign currency risk.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

In certain situations where the Company has forecasted purchases under a long-term commitment or forecasted sales denominated in a foreign currency, Cabot may enter into appropriate financial instruments in accordance with the Company's risk management policy to hedge future cash flow exposures. The following table provides details of the derivatives held as of March 31, 2014 and September 30, 2013 to manage foreign currency risk:

| <u>Description</u> | <u>Borrowing</u> | <u>Notional Amount</u> | | <u>Hedge Designation</u> |
|--|------------------|------------------------|---------------------------|--------------------------|
| | | <u>March 31, 2014</u> | <u>September 30, 2013</u> | |
| Forward Foreign Currency Contracts (1) | N/A | USD 41 million | USD 31 million | No designation |

- (1) Cabot's forward foreign exchange contracts are denominated primarily in the Brazilian real, British pound sterling, Chinese renminbi, Czech koruna, and Indian rupee.

Accounting for Derivative Instruments and Hedging Activities

The Company determines the fair value of derivative instruments using quoted market prices whenever available. When quoted market prices are not available for various types of derivative instruments (such as forwards, options and swaps), the Company uses standard models with market-based inputs, which take into account the present value of estimated future cash flows and the ability of the financial counterparty to perform. For interest rate and cross-currency swaps, the significant inputs to these models are interest rate curves for discounting future cash flows. For forward foreign currency contracts, the significant inputs are interest rate curves for discounting future cash flows, and exchange rate curves of the foreign currency for translating future cash flows.

Fair Value Hedge

For derivative instruments that are designated and qualify as fair value hedges, the gain or loss on the derivative as well as the offsetting gain or loss on the hedged item attributable to the hedged risk are recognized in current period earnings.

Cash Flow Hedge

For derivative instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative is recorded in Accumulated other comprehensive income and reclassified to earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current period earnings.

Other Derivative Instruments

From time to time, the Company may enter into certain derivative instruments that may not be designated as hedges for accounting purposes, which include cross currency swaps, foreign currency forward contracts and commodity derivatives. Although these derivatives do not qualify for hedge accounting, Cabot believes that such instruments are closely correlated with the underlying exposure, thus managing the associated risk. The gains or losses from changes in the fair value of derivative instruments that are not accounted for as hedges are recognized in current period earnings.

For the three and six months ended March 31, 2014 there were no derivatives designated as hedges. For both the three and six months ended March 31, 2013, for derivatives designated as hedges, the change in unrealized gains in Accumulated other comprehensive income, the hedge ineffectiveness recognized in earnings, the realized gains or losses reclassified from Accumulated other comprehensive income, and the losses reclassified from Accumulated other comprehensive income to earnings were immaterial.

During the three and six months ended March 31, 2014, Cabot recognized in earnings through Other (expense) income within the Consolidated Statements of Operations losses of \$2 million and \$4 million, respectively, related to its foreign currency forward contracts, which were not designated as hedges.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

For the three and six months ended March 31, 2013, losses of \$6 million and \$2 million, respectively, were recognized in earnings as a result of the remeasurement to Euros of the \$175 million bond issued by one of Cabot's European subsidiaries. These losses, which were recognized in earnings through Other (expense) income within the Consolidated Statements of Operations, were offset by gains of \$7 million and \$3 million, for the three and six months ended March 31, 2013, respectively, from Cabot's cross currency swaps that are not designated as hedges, but which Cabot entered into to offset the foreign currency translation exposure on the debt. Additionally, during the three and six months ended March 31, 2013, Cabot recognized in earnings through Other (expense) income within the Consolidated Statements of Operations gains of \$3 million and \$9 million, respectively, related to its foreign currency forward contracts, which were not designated as hedges.

For both March 31, 2014 and September 30, 2013, the fair value of derivative instruments were immaterial and were presented in Prepaid expenses and other current assets and Accounts payable and accrued liabilities on the Consolidated Balance Sheets.

The net after-tax amounts to be reclassified from Accumulated other comprehensive income to earnings within the next 12 months are expected to be immaterial.

O. Venezuela

Cabot owns 49% of an operating Carbon Black affiliate in Venezuela, which is accounted for as an equity affiliate, through wholly owned subsidiaries that carry the investment and receive its dividends. As of March 31, 2014, these subsidiaries carried the operating affiliate investment of \$20 million and held 20 million bolivars (less than \$1 million) in cash.

During the six months ended March 31, 2014 and 2013, the operating affiliate declared dividends in the amount of \$4 million and \$2 million, respectively, which were paid in U.S. dollars and repatriated to the Company's wholly owned subsidiaries.

During the second quarter of fiscal 2014, the Venezuelan government enacted several changes to Venezuela's foreign exchange regime, introducing a multi-tier foreign exchange system whereby there are now three exchange rate mechanisms available to convert Venezuelan Bolivars to U.S. dollars. In March 2014, the Venezuelan government created a currency exchange mechanism referred to as SICAD 2 (Supplementary System for the Administration of Foreign Currency) and allowed its use by all entities for all transactions. The exchange rate on March 31, 2014 under SICAD 2 was 50.8 bolivars to the U.S. dollar (B/\$) compared to the previously used official exchange rate of 6.3 B/\$. A significant portion of the Company's operating affiliate's sales are exports denominated in U.S. dollars. The Venezuelan government mandates that a certain percentage of the dollars collected from these sales be converted into Bolivars. Since the exchange rate that was made available to the Company when converting these dollars into Bolivars was 50.8B/\$, the operating affiliate remeasured its bolivar denominated monetary accounts at this rate, resulting in the recognition of a \$2 million loss in the second quarter of fiscal 2014. Cabot's share of the loss was approximately \$1 million, which was included within the Equity in (loss) earnings of affiliated companies line of the Consolidated Statements of Operations.

In addition, the Company remeasured the bolivar denominated monetary accounts in its wholly owned subsidiaries at the SICAD 2 rate as it was determined that this exchange mechanism is applicable to these subsidiaries. This resulted in the recognition of a \$2 million loss in the second quarter of fiscal 2014, which was recorded within Other (expense) income within the Consolidated Statements of Operations. The Company also recognized a tax benefit of \$2 million from a reduction in its bolivar denominated deferred tax liability due to the impact of the devaluation of the bolivar on unremitted earnings.

From a segment reporting perspective, the net impact of the devaluation to the Company's Consolidated Statements of Operations was \$1 million in the second quarter of fiscal 2014.

The operating entity has been profitable historically and has significant export operations from which it is entitled to retain a certain percentage of the foreign currency that it collects, which is principally the U.S. dollar. The Company continues to closely monitor developments in Venezuela and their potential impact on the recoverability of its equity affiliate investment.

The Company closely monitors its ability to convert its bolivar holdings into U.S. dollars, as the Company intends to convert substantially all bolivars held by its wholly owned subsidiaries in Venezuela to U.S. dollars as soon as practical. Any future change in the SICAD 2 rate or opening of additional parallel markets could lead the Company to change the exchange rate it uses and result in gains or losses on the bolivar denominated assets held by its wholly owned subsidiaries.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

P. Financial Information by Segment

The Company identifies a business as an operating segment if: i) it engages in business activities from which it may earn revenues and incur expenses; ii) its operating results are regularly reviewed by the Chief Operating Decision Maker ("CODM") to make decisions about resources to be allocated to the segment and assess its performance; and iii) it has available discrete financial information. The Company has determined that all of its businesses are operating segments. The CODM reviews financial information at the operating segment level to allocate resources and to assess the operating results and financial performance for each operating segment. Operating segments are aggregated into a reportable segment if the operating segments are determined to have similar economic characteristics and if the operating segments are similar in the following areas: i) nature of products and services; ii) nature of production processes; iii) type or class of customer for their products and services; iv) methods used to distribute the products or provide services; and v) if applicable, the nature of the regulatory environment.

The Company has four reportable segments: Reinforcement Materials, Performance Materials, Advanced Technologies and Purification Solutions. Reinforcement Materials represents the Company's Rubber Blacks Business. Purification Solutions represents the Company's Activated Carbon Business. Performance Materials is an aggregation of the Specialty Carbons and Compounds and Fumed Metal Oxides Businesses, which are similar in terms of economic characteristics, nature of products, processes, customer class and product distribution methods.

The Company has combined and disclosed four of its operating segments (Specialty Fluids, Inkjet, Aerogel and Elastomer Composites) into an other reportable segment labeled "Advanced Technologies". The Security Materials business was previously included in the Advanced Technologies reportable segment. During the second quarter of fiscal 2014, as discussed in Note D, the Company reached an agreement to sell its Security Materials business. Accordingly, results of the Security Materials business for all periods presented have been recast as discontinued operations.

Reportable segment operating profit (loss) before interest and taxes ("Segment EBIT") is presented for each reportable segment in the financial information by reportable segment table below on the line entitled Income (loss) from continuing operations before taxes. Segment EBIT excludes certain items, meaning items considered by management to be unusual and not representative of segment results. In addition, Segment EBIT includes Equity in net income of affiliated companies, net of tax, the full operating results of a contractual joint venture in Purification Solutions, royalties, Net income (loss) attributable to noncontrolling interests, net of tax, and discounting charges for certain Notes receivable, but excludes Interest expense, foreign currency transaction gains and losses, interest income, dividend income, unearned revenue, the effects of LIFO accounting for inventory, general unallocated (expense) income and unallocated corporate costs.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

Prior year Purification Solutions Segment EBIT has been adjusted to include an allocation of corporate administrative and functional support costs, which were previously reflected in unallocated corporate costs and other segment results. Beginning in the second quarter of fiscal 2014, a reclassification has been made in the Purification Solutions segment information in order to align the presentation of shipping and handling costs on customer sales with the rest of the Company's businesses. The reclassification was made between Purification Solutions and Unallocated and other to include the shipping and handling costs in Revenues from external customers. There is no impact on Segment EBIT as a result of the reclassification. Historical periods have been adjusted to reflect this reclassification.

Financial information by reportable segment is as follows:

| | Reinforcement Materials | Performance Materials | Advanced Technologies | Purification Solutions | Segment Total | Unallocated and Other ⁽¹⁾ | Consolidated Total |
|---|----------------------------|--------------------------|--------------------------|---------------------------|------------------|---|-----------------------|
| (Dollars in millions) | | | | | | | |
| Three Months Ended March 31, 2014 | | | | | | | |
| Revenues from external customers (2) | \$ 504 | \$ 249 | \$ 48 | \$ 80 | \$ 881 | \$ 17 | \$ 898 |
| Income (loss) from continuing operations before taxes (3) | \$ 61 | \$ 47 | \$ 12 | \$ (4) | \$ 116 | \$ (68) | \$ 48 |
| Three Months Ended March 31, 2013 | | | | | | | |
| Revenues from external customers (2) | \$ 459 | \$ 243 | \$ 39 | \$ 75 | \$ 816 | \$ 24 | \$ 840 |
| Income (loss) from continuing operations before taxes (3) | \$ 42 | \$ 37 | \$ 8 | \$ — | \$ 87 | \$ (50) | \$ 37 |
| Six Months Ended March 31, 2014 | | | | | | | |
| Revenues from external customers (2) | \$ 1,021 | \$ 466 | \$ 112 | \$ 152 | \$ 1,751 | \$ 45 | \$ 1,796 |
| Income (loss) from continuing operations before taxes (3) | \$ 125 | \$ 81 | \$ 37 | \$ (13) | \$ 230 | \$ (73) | \$ 157 |
| Six Months Ended March 31, 2013 | | | | | | | |
| Revenues from external customers (2) | \$ 934 | \$ 439 | \$ 76 | 163 | \$ 1,612 | \$ 47 | \$ 1,659 |
| Income (loss) from continuing operations before taxes (3) | \$ 92 | \$ 64 | \$ 16 | 5 | \$ 177 | \$ (97) | \$ 80 |

(1) Unallocated and Other includes certain items and eliminations necessary to reflect management's reporting of operating segment results. These items are reflective of the segment reporting presented to the Chief Operating Decision Maker.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

- (2) Unallocated and Other reflects royalties, other operating revenues, external shipping and handling costs, the impact of unearned revenue, the removal of 100% of the sales of an equity method affiliate and discounting charges for certain Notes receivable. Details are provided in the table below:

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|---|--------------------------------|--------------|------------------------------|--------------|
| | 2014 | 2013 | 2014 | 2013 |
| | (Dollars in millions) | | | |
| Royalties, other operating revenues, the impact of unearned revenue, the removal of 100% of the sales of an equity method affiliate and discounting charges for certain Notes receivable. | \$ (12) | \$ — | \$ (12) | \$ (3) |
| Shipping and handling costs | 29 | 24 | 57 | 50 |
| Total | \$ 17 | \$ 24 | \$ 45 | \$ 47 |

- (3) Income (loss) from continuing operations before taxes that are categorized as Unallocated and Other includes:

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|--|--------------------------------|----------------|------------------------------|----------------|
| | 2014 | 2013 | 2014 | 2013 |
| | (Dollars in millions) | | | |
| Interest expense | \$ (13) | \$ (16) | \$ (27) | \$ (32) |
| Total certain items, pre-tax(a) | (36) | (20) | (12) | (39) |
| Equity in earnings of affiliated companies, net of tax (b) | — | (3) | (2) | (6) |
| Unallocated corporate costs(c) | (16) | (13) | (29) | (25) |
| General unallocated (expense) income (d) | (3) | 2 | (3) | 5 |
| Total | \$ (68) | \$ (50) | \$ (73) | \$ (97) |

- (a) Certain items are items that management does not consider to be representative of operating segment results and they are, therefore, excluded from Segment EBIT. Certain items, pre-tax, for the three months ended March 31, 2014 include \$16 million related to global restructuring activities, \$6 million of foreign currency loss on revaluations and \$14 million related to legal and environmental matters and reserves. Certain items, pre-tax, for the six months ended March 31, 2014 include \$21 million related to global restructuring activities, \$5 million for acquisition and integration-related charges (consisting of \$3 million for certain other one-time integration costs and \$2 million of additional charges related to acquisition accounting adjustments for the acquired inventory of NHUMO) and \$15 million for legal and environmental matters and reserves offset by a \$29 million non-cash gain recognized on the Company's pre-existing investment in NHUMO as a result of the NHUMO transaction. Certain items, pre-tax, for the three months ended March 31, 2013 include \$19 million related to global restructuring activities and \$2 million for acquisition and integration-related charges offset by \$1 million of foreign currency gain on revaluation. Certain items, pre-tax, for the six months ended March 31, 2013 include \$24 million related to global restructuring activities and \$16 million for acquisition and integration-related charges (consisting of \$5 million for certain other one-time integration costs and \$11 million of charges related to acquisition accounting adjustments for the acquired inventory) offset by \$1 million of foreign currency gain on revaluation.
- (b) Equity in earnings of affiliated companies, net of tax, is included in Segment EBIT and is removed from Unallocated and other to reconcile to income (loss) from continuing operations before taxes.
- (c) Unallocated corporate costs are not controlled by the operating segments and primarily benefit corporate interests.
- (d) General unallocated (expense) income consists of gains (losses) arising from foreign currency transactions, net of other foreign currency risk management activities, the impact of accounting for certain inventory on a LIFO basis, the profit or loss related to the corporate adjustment for unearned revenue, and the impact of including the full operating results of an equity affiliate in Purification Solutions Segment EBIT.

CABOT CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2014
UNAUDITED

Performance Materials is comprised of two businesses that sell the following products: specialty grades of carbon black and thermoplastic concentrates and compounds (the Specialty Carbons and Compounds Business); and fumed silica, fumed alumina and dispersions thereof (the Fumed Metal Oxides Business). The net sales from each of these businesses for the three and six months ended March 31, 2014 and 2013 are as follows:

| | <u>Three Months Ended</u> <u>March 31</u> | | <u>Six Months Ended</u> <u>March 31</u> | |
|---------------------------------|--|---------------|--|---------------|
| | <u>2014</u> | <u>2013</u> | <u>2014</u> | <u>2013</u> |
| | (Dollars in millions) | | | |
| Specialty Carbons and Compounds | \$ 172 | \$ 173 | \$ 320 | \$ 305 |
| Fumed Metal Oxides | 77 | 70 | 146 | 134 |
| Total Performance Materials | <u>\$ 249</u> | <u>\$ 243</u> | <u>\$ 466</u> | <u>\$ 439</u> |

The net sales from each of the Advanced Technologies businesses are as follows:

| | <u>Three Months Ended</u> <u>March 31</u> | | <u>Six Months Ended</u> <u>March 31</u> | |
|-----------------------------|--|--------------|--|--------------|
| | <u>2014</u> | <u>2013</u> | <u>2014</u> | <u>2013</u> |
| | (Dollars in millions) | | | |
| Inkjet Colorants | \$ 14 | \$ 12 | \$ 29 | \$ 28 |
| Aerogel | 1 | 3 | 6 | 8 |
| Elastomer Composites | 8 | 4 | 24 | 12 |
| Specialty Fluids | 25 | 20 | 53 | 28 |
| Total Advanced Technologies | <u>\$ 48</u> | <u>\$ 39</u> | <u>\$ 112</u> | <u>\$ 76</u> |

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**Critical Accounting Policies**

The preparation of our consolidated financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues, and expenses and related disclosure of contingent assets and liabilities. We consider an accounting estimate to be critical to the financial statements if (i) the estimate is complex in nature or requires a high degree of judgment and (ii) different estimates and assumptions were used, the results could have a material impact on the consolidated financial statements. On an ongoing basis, we evaluate our policies and estimates. We base our estimates on historical experience, current conditions and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. The estimates that we believe are critical to the preparation of the consolidated financial statements are presented below.

Revenue Recognition and Accounts Receivable

We recognize revenue when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price is fixed or determinable and collectability is reasonably assured. We generally are able to ensure that products meet customer specifications prior to shipment. If we are unable to determine that the product has met the specified objective criteria prior to shipment or if title has not transferred because of sales terms, the revenue is considered "unearned" and is deferred until the revenue recognition criteria are met. Shipping and handling charges related to sales transactions are recorded as sales revenue when billed to customers or included in the sales price.

The following table shows the relative size of the revenue recognized in each of our reportable segments for the periods presented. The Advanced Technologies reportable segment excludes the Security Materials business from all periods as we began reporting the business under discontinued operations.

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|-------------------------|--------------------------------|------|------------------------------|------|
| | 2014 | 2013 | 2014 | 2013 |
| Reinforcement Materials | 58% | 56% | 58% | 58% |
| Performance Materials | 28% | 30% | 27% | 27% |
| Purification Solutions | 9% | 9% | 9% | 10% |
| Advanced Technologies | 5% | 5% | 6% | 5% |

We derive the substantial majority of revenues from the sale of products in Reinforcement Materials and Performance Materials. Revenue from these products is typically recognized when the product is shipped and title and risk of loss have passed to the customer. We offer certain customers cash discounts and volume rebates as sales incentives. The discounts and volume rebates are recorded as a reduction in sales at the time revenue is recognized and are estimated based on historical experience and contractual obligations. We periodically review the assumptions underlying estimates of discounts and volume rebates and adjust revenues accordingly.

Revenue in Purification Solutions is typically recognized when the product is shipped and title and risk of loss have passed to the customer. For major activated carbon injection systems projects, revenue is recognized using the percentage-of-completion method.

Revenue in Advanced Technologies, excluding the Specialty Fluids Business, is typically recognized when the product is shipped and title and risk of loss have passed to the customer. Depending on the nature of the contract with the customer, a portion of the segment's revenue may be recognized using proportional performance. We have technology and licensing agreements with one customer that are accounted for as multiple element arrangements. Revenue is recognized ratably over the term of the agreements, limited by the cumulative amounts that become due, some of which are through 2022.

[Table of Contents](#)

A significant portion of the revenue in the Specialty Fluids Business, included in Advanced Technologies, arises from the rental of cesium formate. This revenue is recognized throughout the rental period based on the contracted rental terms. Customers are also billed and revenue is recognized, typically at the end of the job, for cesium formate product that is not returned. We also generate revenues from cesium formate sold outside of a rental process and revenue is recognized upon delivery of the fluid.

We maintain allowances for doubtful accounts based on an assessment of the collectability of specific customer accounts, the aging of accounts receivable and other economic information on both an historical and prospective basis. Customer account balances are charged against the allowance when it is probable the receivable will not be recovered. There is no off-balance sheet credit exposure related to customer receivable balances.

Intangible Assets and Goodwill

We record tangible and intangible assets acquired and liabilities assumed in business combinations under the acquisition method of accounting. Amounts paid for an acquisition are allocated to the assets acquired and liabilities assumed based on their fair values at the date of acquisition. Goodwill is comprised of the purchase price of business acquisitions in excess of the fair value assigned to the net tangible and identifiable intangible assets acquired. Goodwill is not amortized but is reviewed for impairment annually as of May 31, or when events or changes in the business environment indicate that the carrying value of the reporting unit may exceed its fair value. A reporting unit, for the purpose of the impairment test, is at or below the operating segment level, and constitutes a business for which discrete financial information is available and regularly reviewed by segment management. The separate businesses included within Performance Materials are considered separate reporting units. The goodwill balance relative to this segment is recorded in the Fumed Metal Oxides reporting unit within Performance Materials.

For the purpose of the goodwill impairment test, we first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying value amount and as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. Alternatively, we may elect to proceed directly to the two-step goodwill impairment test. If an initial qualitative assessment identifies that it is more likely than not that the carrying value of a reporting unit exceeds its estimated fair value, an additional quantitative evaluation is performed under the two-step impairment test. If based on the quantitative evaluation the fair value of the reporting unit is less than its carrying amount, we perform an analysis of the fair value of all assets and liabilities of the reporting unit. If the implied fair value of the reporting unit's goodwill is determined to be less than its carrying amount, an impairment is recognized for the difference. The fair value of a reporting unit is based on discounted estimated future cash flows. The assumptions used to estimate fair value include management's best estimates of future growth rates, operating cash flows, capital expenditures, and discount rates over an estimate of the remaining operating period at the reporting unit level. Should the fair value of any of our reporting units decline because of reduced operating performance, market declines, or other indicators of impairment, or as a result of changes in the discount rate, charges for impairment may be necessary. Based on our most recent annual goodwill impairment test the fair values of all of our reporting units were substantially in excess of their carrying values. We note that the future growth in the Purification Solutions business, which had \$469 million of goodwill at March 31, 2014, is highly dependent on the growth in the mercury removal portion of this business. This growth relies upon achieving the expected volumes and margins in the mercury removal portion of this business and significantly depends on the adoption and enforcement of environmental laws and regulations, particularly those that would require U.S. based coal fired electrical utilities to reduce the quantity of air pollutants they release, including mercury, to comply with the Mercury and Air Toxics Standards that become effective in April 2015.

We use assumptions and estimates in determining the fair value of assets acquired and liabilities assumed in a business combination. The determination of the fair value of intangible assets requires the use of significant judgment with regard to (i) assumptions used in the valuation model; and (ii) determination of the intangible assets' useful lives. We estimate the fair value of identifiable acquisition-related intangible assets principally based on projections of cash flows that will arise from these assets. The projected cash flows are discounted to determine the fair value of the assets at the dates of acquisition. We review definite-lived intangible assets for impairment when indication of potential impairment exists, such as a significant reduction in cash flows associated with the assets. Actual cash flows arising from a particular intangible asset could vary from projected cash flows which could imply different carrying values from those established at the dates of acquisition and which could result in impairment of such asset. We evaluate indefinite-lived intangible assets for impairment annually or when events occur or circumstances change that may reduce the fair value of the asset below its carrying amount. The annual review is performed as of May 31. We may first perform a qualitative assessment to determine whether it is necessary to perform the quantitative impairment test or bypass the qualitative assessment and proceed directly to performing the quantitative impairment test. The quantitative impairment test is based on discounted estimated future cash flows. The assumptions used to estimate fair value include management's best estimates of future growth rates and discount rates over an estimate of the remaining operating period at the unit of accounting level. Our intangible assets are primarily comprised of trademarks, customer relationships, patented and unpatented technology and other intellectual property. Finite lived intangible assets are amortized over their estimated useful lives.

Long-lived Assets

Our long-lived assets primarily include property, plant and equipment, long-term investments and assets held for rent. The carrying values of long-lived assets are reviewed for impairment whenever events or changes in business circumstances indicate that the carrying amount of an asset may not be recoverable. An asset impairment is recognized when the carrying value of the asset is not recoverable based on the probability-weighted undiscounted estimated future cash flows to be generated by the asset. Our estimates reflect management's assumptions about selling prices, production and sales volumes, costs and market conditions over an estimate of the remaining operating period. If an impairment is indicated, the asset is written down to fair value. If the asset does not have a readily determinable market value, a discounted cash flow model may be used to determine the fair value of the asset. The key inputs to the discounted cash flow would be the same as the undiscounted cash flow noted above, with the addition of the discount rate used. In circumstances when an asset does not have separate identifiable cash flows, an impairment charge is recorded when we no longer intend to use the asset.

To test for impairment of assets we generally use a probability-weighted estimate of the future undiscounted net cash flows of the assets over their remaining lives to determine if the value of the asset is recoverable. Long-lived assets are grouped with other assets and liabilities at the lowest level for which independent identifiable cash flows are determinable.

Property, Plant and Equipment

Property, plant and equipment are recorded at cost. Depreciation of property, plant and equipment is calculated using the straight-line method over the estimated useful lives. The depreciable lives for buildings, machinery and equipment, and other fixed assets are twenty to twenty-five years, ten to twenty-five years, and three to twenty-five years, respectively. The cost and accumulated depreciation for property, plant and equipment sold, retired, or otherwise disposed of are removed from the Consolidated Balance Sheets and resulting gains or losses are included in earnings in the Consolidated Statements of Operations. Expenditures for repairs and maintenance are charged to expenses as incurred. Expenditures for major renewals and betterments, which significantly extend the useful lives of existing plant and equipment, are capitalized and depreciated.

Litigation and Contingencies

We are involved in litigation in the ordinary course of business, including personal injury and environmental litigation. After consultation with counsel, as appropriate, we accrue a liability for litigation when it is probable that a liability has been incurred and the amount can be reasonably estimated. The estimated reserves are recorded based on our best estimate of the liability associated with such matters or the low end of the estimated range of liability if we are unable to identify a better estimate within that range. Our best estimate is determined through the evaluation of various information, including claims, settlement offers, demands by government agencies, estimates performed by independent third parties, identification of other responsible parties and an assessment of their ability to contribute, and our prior experience. Litigation is highly uncertain and there is always the possibility of an unusual result in any particular case that may reduce our earnings and cash flows.

The most significant reserves that we have established are for environmental remediation and respirator litigation claims. The amount accrued for environmental matters reflects our assumptions about remediation requirements at the contaminated sites, the nature of the remedies, the outcome of discussions with regulatory agencies and other potentially responsible parties at multi-party sites, and the number and financial viability of other potentially responsible parties. A portion of the reserve for environmental matters is recognized on a discounted basis, which requires the use of an estimated discount rate and estimates of future cash flows associated with the liability. These liabilities can be affected by the availability of new information, changes in the assumptions on which the accruals are based, unanticipated government enforcement action or changes in applicable government laws and regulations, which could result in higher or lower costs.

Our current estimate of the cost of our share of existing and future respirator liability claims is based on facts and circumstances existing at this time and the amount accrued is recognized on a discounted basis. Developments that could affect our estimate include, but are not limited to, (i) significant changes in the number of future claims, (ii) changes in the rate of dismissals without payment of pending silica and non-malignant asbestos claims, (iii) significant changes in the average cost of resolving claims, (iv) significant changes in the legal costs of defending these claims, (v) changes in the nature of claims received, (vi) changes in the law and procedure applicable to these claims, (vii) the financial viability of other parties which contribute to the settlement of respirator claims, (viii) a change in the availability of insurance coverage maintained by the entity from which we acquired the safety respiratory products business or the indemnity provided by its former owner, (ix) changes in the allocation of costs among the various parties paying legal and settlement costs and (x) a determination that the assumptions that were used to estimate our share of liability are no longer reasonable. We cannot determine the impact of these potential developments on our current estimate of our share of liability for these existing and future claims. Accordingly, the actual amount of these liabilities for existing and future claims could be different

[Table of Contents](#)

than the reserved amount. Further, if the timing of our actual payments made for respirator claims differs significantly from our estimated payment schedule, and we determine that we can no longer reasonably predict the timing of such payments, we could then be required to record the reserve amount on an undiscounted basis on our Consolidated Balance Sheets, causing an immediate impact to earnings.

Income Taxes

Our business operations are global in nature, and we are subject to taxes in numerous jurisdictions. Tax laws and tax rates vary substantially in these jurisdictions and are subject to change based on the political and economic climate in those countries. We file our tax returns in accordance with our interpretations of each jurisdiction's tax laws.

Significant judgment is required in determining our worldwide provision for income taxes and recording the related tax assets and liabilities. In the ordinary course of our business, there are operational decisions, transactions, facts and circumstances, and calculations which make the ultimate tax determination uncertain. Furthermore, our tax positions are periodically subject to challenge by taxing authorities throughout the world. We have recorded reserves on uncertain tax position for taxes and associated interest and penalties that may become payable in future years as a result of audits by tax authorities. Any significant impact as a result of changes in underlying facts, law, tax rates, tax audit, or review could lead to adjustments to our income tax expense, our effective tax rate, and/or our cash flow.

We record our tax provision or benefit on an interim basis using an estimated annual effective tax rate. This rate is applied to the current period ordinary income or loss to determine the income tax provision or benefit allocated to the interim period. Losses from jurisdictions for which no benefit can be recognized and the income tax effects of unusual or infrequent items are excluded from the estimated annual effective tax rate and are recognized in the impacted interim period. The estimated annual effective tax rate may be significantly impacted by nondeductible expenses and our projected earnings mix by tax jurisdiction. Adjustments to the estimated annual effective income tax rate are recognized in the period when such estimates are revised.

We record benefits for uncertain tax positions based on an assessment of whether the position is more likely than not to be sustained by the taxing authorities. If this threshold is not met, no tax benefit of the uncertain tax position is recognized. If the threshold is met, the tax benefit that is recognized is the largest amount that is greater than 50% likely of being realized upon ultimate settlement. This analysis presumes the taxing authorities' full knowledge of the positions taken and all relevant facts, but does not consider the time value of money. We also accrue for interest and penalties on these uncertain tax positions and include such charges in the income tax provision in the Consolidated Statements of Operations.

Additionally, we have established valuation allowances against a variety of deferred tax assets, including net operating loss carry forwards, foreign tax credits, and other income tax credits. Valuation allowances take into consideration our ability to use these deferred tax assets and reduce the value of such items to the amount that is deemed more likely than not to be recoverable. Our ability to utilize these deferred tax assets is dependent on achieving our forecast of future taxable operating income over an extended period of time. We review our forecast in relation to actual results and expected trends on a quarterly basis. Failure to achieve our operating income targets may change our assessment regarding the recoverability of our net deferred tax assets and such change could result in a valuation allowance being recorded against some or all of our net deferred tax assets. An increase in a valuation allowance would result in additional income tax expense, while a release of valuation allowances in periods when these tax attributes become realizable would reduce our income tax expense.

Restructuring Activities

Our consolidated financial statements detail specific charges relating to restructuring activities as well as the actual spending that has occurred against the resulting accruals. Our restructuring charges are estimates based on our preliminary assessments of (i) severance and other employee benefits to be granted to employees, which are based on known benefit formulas and identified job grades, (ii) environmental remediation, and (iii) asset impairment and accelerated depreciation. Because these accruals are estimates, they are subject to change as a result of subsequent information that may come to our attention while executing the restructuring plans. These changes in estimates would then be reflected in our consolidated financial statements.

Inventory Valuation

Inventories are stated at the lower of cost or market. The cost of all carbon black inventories in the U.S. is determined using the last-in, first-out (“LIFO”) method. Had we used the first-in, first-out (“FIFO”) method instead of the LIFO method for such inventories, the value of those inventories would have been \$54 million and \$55 million higher as of March 31, 2014 and September 30, 2013, respectively. The cost of Specialty Fluids inventories is determined using the average cost method. The cost of other U.S. and non-U.S. inventories is determined using the FIFO method. In periods of rapidly rising or declining raw material costs, the inventory method we employ can have a significant impact on our profitability. Under our current LIFO method, when raw material costs are rising, our most recent higher priced purchases are the first to be charged to cost of sales. If, however, we were using a FIFO method, our purchases from earlier periods, which were at lower prices, would instead be the first charged to cost of sales. The opposite result could occur during a period of rapid decline in raw material costs.

We review inventory for both potential obsolescence and potential loss of value periodically. In this review, we make assumptions about the future demand for and market value of our inventory and based on these assumptions estimate the amount of any obsolete, unmarketable or slow moving inventory. We write down the value of our inventories by an amount equal to the difference between the cost of the inventory and its estimated market value. Historically, such write-downs have not been significant. If actual market conditions are less favorable than those projected by management at the time of the assessment, however, additional inventory write-downs may be required, which could reduce our gross profit and our earnings.

Results of Operations

Definition of Terms and Non-GAAP Financial Measures

When discussing our results of operations, we use several terms as described below.

The term “product mix” refers to the various types and grades, or mix, of products sold in a particular business or segment during the period, and the positive or negative impact of that mix on the revenue or profitability of the business or segment.

The discussion under the heading “Provision for Income Taxes and Reconciliation of Effective Tax Rate to Operating Tax Rate” includes a discussion of our “effective tax rate” and our “operating tax rate” and includes a reconciliation of the two rates. Our operating tax rate is a non-GAAP financial measure and should not be considered as an alternative to our effective tax rate, the most comparable GAAP financial measure. In calculating our operating tax rate, we exclude discrete tax items, which include: i) unusual or infrequent items such as a significant release of a valuation allowance, ii) items related to uncertain tax positions such as the tax impact of audit settlements, interest on tax reserves, and the release of tax reserves from the expiration of statutes of limitations, and iii) other discrete tax items, such as the tax impact of legislative changes and, on a quarterly basis, the timing of losses in certain jurisdictions and the cumulative rate adjustment, if applicable. We also exclude the tax impact of certain items, as defined below in the discussion of Total segment EBIT, on both operating income and the tax provision. Our definition of the operating tax rate may not be comparable to the definition used by other companies. Management believes that the non-GAAP financial measure is useful supplemental information because it helps our investors compare our tax rate year to year on a consistent basis and understand what our tax rate on current operations would be without the impact of these items which we do not believe are reflective of the underlying business results.

Total segment EBIT is a non-GAAP performance measure, and should not be considered an alternative for Income from continuing operations before taxes, the most directly comparable GAAP financial measure. In calculating Total segment EBIT, we make certain adjustments such as excluding certain items, meaning items that management does not consider representative of our fundamental segment results, as well as items that are not allocated to our business segments, such as interest expense and other corporate costs. Our Chief Operating Decision Maker uses segment EBIT to evaluate the operating results of each segment and to allocate resources to the segments. We believe Total segment EBIT provides useful supplemental information for our investors as it is an important indicator of the Company’s operational strength and performance. Investors should consider the limitations associated with this non-GAAP measure, including the potential lack of comparability of this measure from one company to another. A reconciliation of Total segment EBIT to Income from continuing operations before income taxes and equity in earnings of affiliated companies is provided in Note P of our consolidated financial statements.

Cabot is organized into four reportable business segments: Reinforcement Materials, Performance Materials, Advanced Technologies and Purification Solutions. Cabot is also organized for operational purposes into three geographic regions: the Americas; Europe, Middle East and Africa; and Asia Pacific. Discussions of all periods reflect these structures.

[Table of Contents](#)

Our analysis of financial condition and operating results should be read with our consolidated financial statements and accompanying notes.

Overview

During the second quarter of fiscal 2014, Income from continuing operations before income taxes and equity in earnings of affiliated companies increased compared to the second quarter of fiscal 2013 largely due to higher volumes as demand in our key end markets improved and from the addition of new carbon black capacity in China and Mexico.

During the first six months of fiscal 2014, Income from continuing operations before income taxes and equity in earnings of affiliated companies increased compared to the first six months of fiscal 2013 largely due to higher volumes and a gain recognized on our pre-existing equity investment in our carbon black joint venture in Mexico, NHUMO, S.A. de C.V. ("NHUMO"), with Grupo Kuo S.A.B. de C.V. ("KUO"), from our acquisition during the first quarter of fiscal 2014 of KUO's common stock interest in NHUMO. See Note C to our consolidated financial statements for details of the NHUMO transaction.

Second Quarter and First Six Months Fiscal 2014 versus Second Quarter and First Six Months Fiscal 2013—Consolidated

Net Sales and other operating revenues and Gross Profit

| | Three Months Ended | | Six Months Ended | |
|--|-----------------------|--------|-----------------------|----------|
| | March 31 | | March 31 | |
| | 2014 | 2013 | 2014 | 2013 |
| | (Dollars in millions) | | (Dollars in millions) | |
| Net sales and other operating revenues | \$ 898 | \$ 840 | \$ 1,796 | \$ 1,659 |
| Gross profit | \$ 176 | \$ 143 | \$ 355 | \$ 290 |

The \$58 million increase in net sales from the second quarter of fiscal 2013 to the second quarter of fiscal 2014 was due primarily to higher volumes (\$80 million) partially offset by a less favorable price and product mix (combined \$13 million) and an unfavorable impact from foreign currency translation (\$5 million). For the first six months of fiscal 2014, net sales increased by \$137 million when compared to the same period of fiscal 2013. The increase was driven primarily by higher volumes (\$185 million) partially offset by a less favorable price and product mix (combined \$39 million) and an unfavorable impact from foreign currency translation (\$12 million).

Gross profit increased by \$33 million in the second quarter of fiscal 2014 and by \$65 million in the first six months of fiscal 2014 when compared to the same periods of fiscal 2013 primarily due to higher volumes.

[Table of Contents](#)*Selling and Administrative Expenses*

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|-------------------------------------|--------------------------------|-------|------------------------------|--------|
| | 2014 | 2013 | 2014 | 2013 |
| | (Dollars in millions) | | (Dollars in millions) | |
| Selling and administrative expenses | \$ 92 | \$ 77 | \$ 169 | \$ 150 |

Selling and administrative expenses increased by \$15 million in the second quarter of fiscal 2014 and \$19 million in the first six months of fiscal 2014 when compared to the same periods of fiscal 2013. The increases in both periods were principally driven by higher expenses related to restructuring actions taken in our Europe, Middle East and Africa ("EMEA") shared service center, the addition of NHUMO, and higher costs associated with corporate projects.

Research and Technical Expenses

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|---------------------------------|--------------------------------|-------|------------------------------|-------|
| | 2014 | 2013 | 2014 | 2013 |
| | (Dollars in millions) | | (Dollars in millions) | |
| Research and technical expenses | \$ 16 | \$ 16 | \$ 31 | \$ 33 |

Research and technical expenses was consistent in the second quarter of fiscal 2014 as compared to the same period in fiscal 2013. Research and technical expenses decreased by \$2 million in the first six months of fiscal 2014 when compared to the same period of fiscal 2013. The decrease was driven by lower costs from restructuring-related activities undertaken in the prior year.

Interest and Dividend Income, Interest Expense and Other (Expense) Income

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|------------------------------|--------------------------------|-------|------------------------------|-------|
| | 2014 | 2013 | 2014 | 2013 |
| | (Dollars in millions) | | (Dollars in millions) | |
| Interest and dividend income | \$ 1 | \$ 1 | \$ 2 | \$ 2 |
| Interest expense | \$ 13 | \$ 16 | \$ 27 | \$ 32 |
| Other (expense) income | \$ (8) | \$ 2 | \$ 27 | \$ 3 |

Interest and dividend income was consistent in both the second quarter and first six months of fiscal 2014 as compared to the same periods in fiscal 2013.

Interest expense decreased by \$3 million in the second quarter and by \$5 million during the first six months of fiscal 2014 when compared to the same periods in fiscal 2013 due to the maturity of long-term debt in the fourth quarter of fiscal 2013 that was refinanced with commercial paper carrying a lower interest rate.

Other (expense) income in the second quarter decreased by \$10 million due principally to an unfavorable comparison of foreign currency movements (\$9 million) driven primarily by the devaluations of the Venezuelan bolivar and Argentinian peso during the second quarter of fiscal 2014. In the first six months of fiscal 2014, Other (expense) income increased by \$24 million as compared to the same period in fiscal 2013 due primarily to a gain recognized on our existing equity investment in NHUMO (\$29 million) as a result of the NHUMO transaction. This gain was partially offset by an unfavorable comparison of foreign currency movements (\$3 million).

[Table of Contents](#)

Provision for Income Taxes and Reconciliation of Effective Tax Rate to Operating Tax Rate

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|--|--------------------------------|------------|------------------------------|------------|
| | 2014 | 2013 | 2014 | 2013 |
| | (Dollars in millions) | | (Dollars in millions) | |
| Provision for income taxes | \$ 7 | \$ 16 | \$ 31 | \$ 36 |
| Effective tax rate | 14% | 43% | 20% | 45% |
| Impact of discrete tax items: | | | | |
| (1) Unusual or infrequent items | 1% | (9%) | — % | (13%) |
| (2) Items related to uncertain tax positions | 11% | 7% | 4% | 3% |
| (3) Other discrete tax items | (3%) | 4% | (1%) | — % |
| Impact of certain items | 5% | (18%) | 5% | (8%) |
| Operating tax rate | <u>28%</u> | <u>27%</u> | <u>28%</u> | <u>27%</u> |

During the second quarter of fiscal 2014, we recorded a tax provision of \$7 million, resulting in an effective tax rate of 14%. This amount included net discrete tax benefits of \$4 million. The operating rate for the second quarter of fiscal 2014 was 28%. During the second quarter of fiscal 2013, we recorded a tax provision of \$16 million, resulting in an effective tax rate of 43%. This amount included a net discrete tax charge of less than \$1 million. The operating tax rate for the second quarter of fiscal 2013 was 27%. The increase in the operating tax rate in the second quarter of fiscal 2014 is primarily due to the expiration of the research and experimentation credit in the U.S. and a change in our geographic mix of earnings.

For the first six months of fiscal 2014, we recorded a tax provision of \$31 million, resulting in an effective tax rate of 20%. This amount included net discrete benefits of \$3 million. For the first six months of fiscal 2013, we recorded a net tax provision of \$36 million, resulting in an effective tax rate of 45%. This amount included a net discrete tax charge of \$7 million. The decrease in the effective tax rate in the first six months of fiscal 2014 is primarily due to a non-taxable gain of \$29 million recognized on the Company's pre-existing investment in NHUMO as a result of the NHUMO transaction. This gain is reported as a certain item. See Note C of the consolidated financial statements for details of the transaction. The increase in the operating tax rate for the first six months of fiscal 2014 is primarily due to the expiration of the research and experimentation credit in the U.S. and a change in our geographic mix of earnings.

We are currently under audit in a number of jurisdictions outside of the U.S. It is possible that some of these audits will be resolved in fiscal 2014, which may impact our tax expense and effective tax rate going forward. We expect our operating tax rate for fiscal 2014 to be approximately 28%.

Equity in (Loss) Earnings of Affiliated Companies and Net Income (Loss) Attributable to Noncontrolling Interests

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|--|--------------------------------|--------|------------------------------|------|
| | 2014 | 2013 | 2014 | 2013 |
| | (Dollars in millions) | | (Dollars in millions) | |
| Equity in (loss) earnings of affiliated companies, net of tax | \$ (2) | \$ 3 | \$ — | \$ 6 |
| Net income (loss) attributable to noncontrolling interests, net of tax | \$ 3 | \$ (4) | \$ 9 | \$ — |

Equity in (loss) earnings of affiliated companies, net of tax, decreased \$5 million in the second quarter and \$6 million in the first six months of fiscal 2014 when compared to the same periods of fiscal 2013. The declines in both periods were due to the consolidation of the earnings of NHUMO following the NHUMO transaction and lower earnings from our Venezuelan equity affiliate, including the unfavorable impact on monetary assets from the devaluation of the Venezuelan bolivar.

Net income (loss) attributable to noncontrolling interests, net of tax, increased \$7 million in the second quarter of fiscal 2014 and \$9 million in the first six months of fiscal 2014 as compared to the same periods of fiscal 2013. The increases in both comparative periods were due to higher profitability of our joint ventures and charges associated with our 2013 restructuring in Malaysia that did not repeat in fiscal 2014.

Net Income Attributable to Cabot Corporation

In the second quarter and first six months of fiscal 2014, we reported net income attributable to Cabot Corporation of \$36 million and \$116 million, respectively (\$0.54 and \$1.77 per diluted common share, respectively). This is compared to \$27 million and \$47 million, respectively (\$0.42 and \$0.73 per diluted common share, respectively) in the second quarter and first six months of fiscal 2013.

Second Quarter Fiscal 2014 versus Second Quarter Fiscal 2013—By Business Segment

Total segment EBIT, certain items, other unallocated items and Income from continuing operations before income taxes and equity in earnings of affiliated companies for the three and six months ended March 31, 2014 and 2013 are set forth in the table below. The details of certain items and other unallocated items are shown below and in Note P of our consolidated financial statements.

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|--|--------------------------------|--------------|------------------------------|--------------|
| | 2014 | 2013 | 2014 | 2013 |
| | (Dollars in millions) | | (Dollars in millions) | |
| Total segment EBIT | \$ 116 | \$ 87 | \$ 230 | \$ 177 |
| Certain items | (36) | (20) | (12) | (39) |
| Other unallocated items | (32) | (30) | (61) | (58) |
| Income from continuing operations before income taxes and equity in earnings of affiliated companies | <u>\$ 48</u> | <u>\$ 37</u> | <u>\$ 157</u> | <u>\$ 80</u> |

In the second quarter of fiscal 2014, total segment EBIT increased by \$29 million when compared to the same period of fiscal 2013. The increase was principally driven by higher volumes (\$29 million), higher unit margins (\$11 million), higher royalties and technology payments in Elastomer Composites (\$4 million) and a favorable impact of foreign currency translation (\$3 million). These improvements were partially offset by higher fixed costs (\$16 million) driven by costs from new capacity in the Reinforcement Materials segment. Equity in earnings of affiliated companies decreased (\$5 million) due to the consolidation of earnings following the NHUMO transaction and lower earnings from our Venezuelan equity affiliate.

In the first six months of fiscal 2014, total segment EBIT increased by \$53 million when compared to the same period of fiscal 2013. The increase was principally driven by higher volumes (\$72 million), higher unit margins (\$9 million) and higher royalties and technology payments in Elastomer Composites (\$9 million). These improvements were partially offset by higher fixed costs (\$36 million) driven by costs from new capacity in the Reinforcement Materials segment and higher maintenance costs in the Purification Solutions segment. Equity in earnings of affiliated companies decreased (\$6 million) due to the consolidation of earnings following the NHUMO transaction and lower earnings from our Venezuelan equity affiliate.

[Table of Contents](#)

Certain Items

Details of the certain items for the second quarter and first six months of fiscal 2014 and 2013 are as follows:

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|---|--------------------------------|---------|------------------------------|---------|
| | 2014 | 2013 | 2014 | 2013 |
| | (Dollars in millions) | | (Dollars in millions) | |
| Global restructuring activities | \$ (16) | \$ (19) | \$ (21) | \$ (24) |
| Acquisition and integration-related charges | — | (2) | (5) | (16) |
| Foreign currency (loss) gain on revaluations | (6) | 1 | — | 1 |
| Gain on existing investment in NHUMO | — | — | 29 | — |
| Legal and environmental matters and reserves | (14) | — | (15) | — |
| Total certain items, pre-tax | (36) | (20) | (12) | (39) |
| Tax-related certain items | | | | |
| Tax impact of certain items | 13 | (1) | 14 | 5 |
| Tax impact of certain foreign exchange losses | — | (5) | — | (12) |
| Discrete tax items | 4 | 5 | 3 | 5 |
| Total tax-related certain items | 17 | (1) | 17 | (2) |
| Total certain items after tax | \$ (19) | \$ (21) | \$ 5 | \$ (41) |

Certain items for the second quarter and first six months of fiscal 2014 include charges related to restructuring activities, acquisition and integration-related charges, foreign currency impacts on revaluations, a gain recognized on our existing equity investment in NHUMO, legal and environmental matters and reserves and tax certain items. Details of restructuring activities are included in Note L of the consolidated financial statements. Acquisition and integration-related charges include legal and professional fees, the incremental value of inventory as a result of purchase accounting adjustments, and other expenses related to the completion of the acquisitions and the integrations of Purification Solutions and NHUMO. Details of the gain recognized on our existing equity investment in NHUMO are included in Note C of the consolidated financial statements. A discussion of legal and environmental matters and reserves is included in Note I of the consolidated financial statements. Tax-related certain items include discrete tax items, which are unusual and infrequent, and the tax impact of certain foreign exchange losses.

Other Unallocated Items

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|--|--------------------------------|---------|------------------------------|---------|
| | 2014 | 2013 | 2014 | 2013 |
| | (Dollars in millions) | | (Dollars in millions) | |
| Interest expense | \$ (13) | \$ (16) | \$ (27) | \$ (32) |
| Equity in earnings of affiliated companies | — | (3) | (2) | (6) |
| Unallocated corporate costs | (16) | (13) | (29) | (25) |
| General unallocated (expense) income | (3) | 2 | (3) | 5 |
| Total other unallocated items | \$ (32) | \$ (30) | \$ (61) | \$ (58) |

Costs from total other unallocated items increased by \$2 million in the second quarter of fiscal 2014 as compared to the same period in fiscal 2013. The increase was driven by a \$5 million increase in General unallocated (expense) income primarily due to the unfavorable comparison of foreign currency transactions (\$3 million) and \$3 million higher Unallocated corporate costs associated with corporate projects. These increases were partially offset by \$3 million lower equity in earnings of affiliated companies, net of tax, due to the consolidation of the earnings of NHUMO following the NHUMO transaction and lower earnings from our Venezuelan equity affiliate. Interest expense also decreased by \$3 million due to the maturity of long-term debt in the fourth quarter of fiscal 2013 that was refinanced with commercial paper carrying a lower interest rate.

[Table of Contents](#)

In the first six months of fiscal 2014, costs from Total other unallocated items increased by \$3 million when compared to the same period of fiscal 2013. The increase was driven by a \$8 million increase in General unallocated (expense) income primarily due to the unfavorable comparison of foreign currency transactions (\$4 million) and \$4 million higher Unallocated corporate costs associated with corporate projects. These increases were partially offset by \$4 million lower equity in earnings of affiliated companies, net of tax, due to the consolidation of the earnings of NHUMO following the NHUMO transaction and lower earnings from our Venezuelan equity affiliate. Interest expense also decreased by \$5 million due to the maturity of long-term debt in the fourth quarter of fiscal 2013 that was refinanced with commercial paper carrying a lower interest rate.

Reinforcement Materials

Sales and EBIT for Reinforcement Materials for the second quarter and first six months of fiscal 2014 and fiscal 2013 are as follows:

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|-------------------------------|--------------------------------|--------|------------------------------|--------|
| | 2014 | 2013 | 2014 | 2013 |
| | (Dollars in millions) | | (Dollars in millions) | |
| Reinforcement Materials Sales | \$ 504 | \$ 459 | \$ 1,021 | \$ 934 |
| Reinforcement Materials EBIT | \$ 61 | \$ 42 | \$ 125 | \$ 92 |

In the second quarter of fiscal 2014, sales in Reinforcement Materials increased by \$45 million when compared to the second quarter of fiscal 2013. The increase was principally driven by the impact of higher volumes (\$67 million) partially offset by a less favorable price and product mix (combined \$15 million) and an unfavorable impact from foreign currency translation (\$6 million). In the first six months of fiscal 2014, sales in Reinforcement Materials increased by \$87 million when compared to the first six months of fiscal 2013. The increase was principally driven by higher volumes (\$139 million) partially offset by a less favorable price and product mix (combined \$37 million) and an unfavorable impact from foreign currency translation (\$15 million). Higher volumes in both comparative periods were due to improved carbon black demand and the addition of new capacity in China and Mexico. The less favorable price and product mix in both comparative periods were primarily due to price adjustments to customers for decreases in raw material costs.

EBIT in Reinforcement Materials increased by \$19 million in the second quarter of fiscal 2014 when compared to the same period of fiscal 2013. The increase was principally driven by 15% higher volumes (\$22 million) and favorable unit margins (\$8 million) partially offset by higher fixed costs (\$11 million). For the first six months of fiscal 2014 when compared to the same period of fiscal 2013, Reinforcement Materials EBIT increased by \$33 million driven principally by higher volumes (\$45 million) and favorable unit margins (\$7 million) partially offset by higher fixed costs (\$20 million). Higher volumes in both comparative periods were due to improved carbon black demand and the addition of new capacity in China and Mexico. Favorable unit margins in both comparative periods were most notably due to raw material purchasing savings and the benefits from energy efficiency investments. Higher fixed costs for both comparative periods were primarily associated with new carbon black capacity in China and Mexico.

Performance Materials

Sales and EBIT for Performance Materials for the second quarter and first six months of fiscal 2014 and fiscal 2013 are as follows:

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|---------------------------------------|--------------------------------|--------|------------------------------|--------|
| | 2014 | 2013 | 2014 | 2013 |
| | (Dollars in millions) | | (Dollars in millions) | |
| Specialty Carbons and Compounds Sales | \$ 172 | \$ 173 | \$ 320 | \$ 305 |
| Fumed Metal Oxides Sales | 77 | 70 | 146 | 134 |
| Performance Materials Sales | \$ 249 | \$ 243 | \$ 466 | \$ 439 |
| Performance Materials EBIT | \$ 47 | \$ 37 | \$ 81 | \$ 64 |

[Table of Contents](#)

In the second quarter of fiscal 2014, sales for Performance Materials increased by \$6 million when compared to the second quarter of fiscal 2013. The increase was due to higher volumes (\$7 million) and the favorable impact of foreign currency translation (\$2 million) partially offset by a less favorable price and product mix (combined \$2 million). Volumes in Specialty Carbons and Compounds increased by 3% and volumes in Fumed Metal Oxides increased by 4%. During the first six months of fiscal 2014, sales in Performance Materials increased by \$27 million primarily due to the higher volumes (\$32 million) and a favorable impact of foreign currency translation (\$4 million) partially offset by a less favorable price and product mix (combined \$8 million). Higher volumes in both comparative periods were due to improved demand in our key end markets. The less favorable price and product mix in both comparative periods were primarily due to price adjustments to customers that coincided with decreases in raw material costs in our Specialty Carbons and Compounds business.

EBIT in Performance Materials increased by \$10 million in the second quarter of fiscal 2014 when compared to the same quarter of fiscal 2013 principally due to higher volumes (\$4 million), favorable unit margins (\$4 million) and the favorable impact of foreign currency translation (\$1 million). For the first six months of fiscal 2014, EBIT was \$17 million higher when compared to the first six months of fiscal 2013 driven by higher volumes (\$17 million). Higher volumes in both comparative periods were due to improved demand in our key end markets. The favorable unit margins in the second quarter of fiscal 2014 when compared to the second quarter of fiscal 2013 were primarily due to improved pricing and product mix in our Fumed Metal Oxides business.

Advanced Technologies

Sales and EBIT for Advanced Technologies for the second quarter and first six months of fiscal 2014 and 2013 are as follows:

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|-----------------------------|--------------------------------|--------------|------------------------------|--------------|
| | 2014 | 2013 | 2014 | 2013 |
| | (Dollars in millions) | | (Dollars in millions) | |
| Inkjet Colorants | \$ 14 | \$ 12 | \$ 29 | \$ 28 |
| Aerogel | 1 | 3 | 6 | 8 |
| Elastomer Composites | 8 | 4 | 24 | 12 |
| Specialty Fluids | 25 | 20 | 53 | 28 |
| Advanced Technologies Sales | <u>\$ 48</u> | <u>\$ 39</u> | <u>\$ 112</u> | <u>\$ 76</u> |
| Advanced Technologies EBIT | <u>\$ 12</u> | <u>\$ 8</u> | <u>\$ 37</u> | <u>\$ 16</u> |

Sales in Advanced Technologies increased by \$9 million in the second quarter of fiscal 2014 when compared to the same period of fiscal 2013 primarily due to higher volumes (\$10 million) and higher royalties in Elastomer Composites (\$4 million) partially offset by an unfavorable price and product mix (\$4 million). In the first six months of fiscal 2014, sales in Advanced Technologies increased by \$36 million when compared to the first six months of fiscal 2013 due to higher volumes (\$33 million) and higher royalties and technology payments in Elastomer Composites (\$9 million) partially offset by lower Aerogel royalties (\$3 million). Higher volumes in both comparative periods were driven by an increased level of rental and sales activity in Specialty Fluids.

EBIT in Advanced Technologies increased by \$4 million in the second quarter of fiscal 2014 when compared to the same period of fiscal 2013 due to higher volumes (\$6 million) and higher royalties and technology payments in Elastomer Composites (\$4 million). These favorable items were partially offset by a less favorable price and product mix (\$3 million) and higher costs (\$2 million) both related to Specialty Fluids. For the first six months of fiscal 2014 when compared to the same period of fiscal 2013, Advanced Technologies EBIT increased by \$21 million driven principally by higher volumes (\$19 million), most notably in Specialty Fluids and Inkjet Colorants, and higher royalties and technology payments in Elastomer Composites (\$9 million). These items were partially offset by higher costs (\$5 million) in Specialty Fluids and lower Aerogel royalties (\$3 million).

Purification Solutions

Sales and EBIT for Purification Solutions for the second quarter and first six months of fiscal 2014 and fiscal 2013 are as follows:

| | Three Months Ended March 31 | | Six Months Ended March 31 | |
|------------------------------|--------------------------------|-------|------------------------------|--------|
| | 2014 | 2013 | 2014 | 2013 |
| | (Dollars in millions) | | (Dollars in millions) | |
| Purification Solutions Sales | \$ 80 | \$ 75 | \$ 152 | \$ 163 |
| Purification Solutions EBIT | \$ (4) | \$ — | \$ (13) | \$ 5 |

Sales in Purification Solutions increased by \$5 million in the second quarter of fiscal 2014 when compared to the same period of fiscal 2013 due to a favorable price and product mix (combined \$9 million) partially offset by lower volumes (\$4 million). During the first six months of fiscal 2014, sales in Purification Solutions decreased by \$11 million primarily due to lower volumes (\$18 million) partially offset by a favorable price and product mix (combined \$8 million). The favorable price and product mix in both comparative periods were primarily due to the implementation of price increases. Lower volumes in both comparative periods were driven by a decline in demand in the air and gas sector.

EBIT in Purification Solutions decreased by \$4 million in the second quarter of fiscal 2014 when compared to the same quarter of fiscal 2013 due to lower volumes (\$2 million) and higher fixed costs (\$4 million). These items were partially offset by favorable pricing and product mix (combined \$2 million). For the first six months of fiscal 2014, EBIT was \$18 million lower when compared to the first six months of fiscal 2013 driven by lower volumes (\$9 million) and higher fixed costs (\$11 million), partially offset by a favorable price and product mix (\$2 million). Lower volumes in both comparative periods were driven by a decline in demand in the air and gas sector. Higher fixed costs in both comparative periods were primarily related to higher maintenance costs and a higher allocation of certain functional and indirect costs. The favorable price and product mix in both comparative periods were primarily due to the implementation of price increases.

Cash Flows and Liquidity

Overview

Our liquidity position, as measured by cash and cash equivalents plus borrowing availability decreased by \$116 million during the first six months of fiscal 2014. The decrease was largely attributable to the acquisition of NHUMO and an increase in working capital. At March 31, 2014, we had cash and cash equivalents of \$89 million, and current availability under our revolving credit agreement of approximately \$398 million. Our revolving credit agreement, which has a \$750 million limit, supports our commercial paper program. The aggregate borrowings under both our commercial paper program and revolving credit agreement cannot exceed the \$750 million limit. The outstanding balance of commercial paper as of March 31, 2014 was \$352 million and is included within the Notes payable caption on our Consolidated Balance Sheets. Our revolving credit agreement contains affirmative, negative and financial covenants and events of default customary for financings of this type. The financial covenants in the revolving credit agreement include interest coverage, debt-to-EBITDA and subsidiary debt to total capitalization ratios. As of March 31, 2014, we were in compliance with all applicable covenants.

We generally manage our cash and debt on a global basis to provide for working capital requirements as needed by region or site. Cash and debt are generally denominated in the local currency of the subsidiary holding the assets or liabilities, except where there are operational cash flow reasons to hold non-functional currency or debt. As of March 31, 2014, our U.S. dollar equivalent cash and cash equivalent holdings by region were: Asia Pacific \$50 million, Europe \$15 million, and the Americas \$24 million, which included \$3 million in the U.S. As discussed in more detail below in the Discontinued Operations section, we received \$215 million of cash during the first week of April 2014 on notes receivable related to the fiscal 2012 sale of our former Supermetals Business.

We anticipate sufficient liquidity from (i) cash on hand; (ii) cash flows from operating activities; and (iii) cash available from our revolving credit agreement and our commercial paper program to meet our operational and capital investment needs and financial obligations for the foreseeable future. Our liquidity derived from cash flows from operations is, to a large degree, predicated on our ability to collect our receivables in a timely manner, the cost of our raw materials, and our ability to manage inventory levels.

[Table of Contents](#)

Discontinued Operations

Our Consolidated Statements of Cash Flows have been presented to include discontinued operations with continuing operations. Therefore, unless noted otherwise, the following discussion of our cash flows and liquidity position include both continuing and discontinued operations.

In January 2012, we completed the sale of our Supermetals Business to GAM. At March 31, 2014, we had Notes receivable from the sale of the business of \$215 million related to the GAM Notes recorded in our Consolidated Balance Sheets. We received the full \$215 million of cash from GAM during the first week of April 2014.

The following discussion of the changes in our cash balance refers to the various sections of our Consolidated Statements of Cash Flows.

Cash Flows from Operating Activities

Cash provided by operating activities, which consists of net income adjusted for the various non-cash items included in income, changes in working capital and changes in certain other balance sheet accounts, totaled \$69 million in the first six months of fiscal 2014, compared to \$4 million during the same period of fiscal 2013.

Cash provided by operating activities in the first six months of fiscal 2014 was driven primarily by net income of \$125 million plus \$100 million of depreciation and amortization and \$21 million of dividends from equity affiliates. These sources of cash were partially offset by a net increase in working capital (inventories plus accounts and notes receivable, less accounts payable and accrued liabilities). Our working capital increase during the first six months of fiscal 2014 was driven primarily by higher accounts receivable, higher inventories and lower accounts payable and accrued liabilities.

Cash generated from operating activities in the first six months of fiscal 2013 was driven primarily by net income of \$47 million plus \$99 million of depreciation and amortization. These sources of cash were partially offset by a net increase in working capital (inventories plus accounts and notes receivable, less accounts payable and accrued liabilities) and a decrease in income taxes payable. Our working capital increase during the first six months of fiscal 2013 was driven primarily by higher inventories and lower accounts payable and accrued liabilities due to the timing and payout of certain corporate accruals.

Cash Flows from Investing Activities

In the six months ended March 31, 2014, investing activities consumed \$148 million of cash and were primarily driven by capital expenditures of \$70 million and cash paid for the NHUMO acquisition of \$73 million (net of cash acquired of \$7 million). For the six months ended March 31, 2013, investing activities consumed \$101 million of cash and were primarily driven by capital expenditures partially offset by \$30 million of cash received from notes receivable from the sale of the Supermetals business.

During the six months ended March 31, 2014, capital expenditures were primarily related to sustaining and compliance capital projects at our operating facilities, site development at our mine in Marshall, Texas, to support the future raw materials supply for the Purification Solutions business, investments in energy recovery technology, and capital spending required for process technology and product differentiation projects.

Capital expenditures for the remainder of fiscal 2014 are expected to be between \$130 million to \$180 million. Our planned capital spending program for the remainder of fiscal 2014 is primarily for sustaining and compliance capital projects at our operating facilities, investments in energy related projects, and site-development initiatives.

Cash Flows from Financing Activities

In the six months ended March 31, 2014, financing activities provided \$89 million primarily related to net inflows of \$111 million from our commercial paper program. In the first six months of fiscal 2014, our overall debt balance increased by \$121 million primarily driven by the acquisition of NHUMO, capital expenditures and working capital increases.

During the first six months of fiscal 2013, financing activities provided \$69 million of cash. We received net inflows of \$256 million from our commercial paper program, and used the majority of the proceeds to repay \$189 million on our revolving credit agreement. In the first six months of fiscal 2013, our overall debt balance increased by \$93 million to fund capital expenditures and working capital requirements.

Venezuela

We own 49% of an operating Carbon Black affiliate in Venezuela, which is accounted for as an equity affiliate, through wholly owned subsidiaries that carry the investment and receive its dividends. As of March 31, 2014, these subsidiaries carried the operating affiliate investment of \$20 million and held 20 million bolivars (less than \$1 million) in cash.

During the six months ended March 31, 2014 and 2013, the operating affiliate declared dividends in the amount of \$4 million and \$2 million, respectively, which were paid in U.S. dollars and repatriated to our wholly owned subsidiaries.

During the second quarter of fiscal 2014, the Venezuelan government enacted several changes to Venezuela's foreign exchange regime, introducing a multi-tier foreign exchange system whereby there are now three exchange rate mechanisms available to convert Venezuelan Bolivars to U.S. dollars. In March 2014, the Venezuelan government created a currency exchange mechanism referred to as SICAD 2 (Supplementary System for the Administration of Foreign Currency) and allowed its use by all entities for all transactions. The exchange rate on March 31, 2014 under SICAD 2 was 50.8 bolivars to the U.S. dollar (B/\$) compared to the previously used official exchange rate of 6.3 B/\$. A significant portion of our operating affiliate's sales are exports denominated in U.S. dollars. The Venezuelan government mandates that a certain percentage of the dollars collected from these sales be converted into Bolivars. Since the exchange rate that was made available to us when converting these dollars into Bolivars was 50.8B/\$, the operating affiliate remeasured its bolivar denominated monetary accounts at this rate, resulting in the recognition of a \$2 million loss in the second quarter of fiscal 2014. Our share of the loss was approximately \$1 million, which was included within the Equity in (loss) earnings of affiliated companies line of the Consolidated Statements of Operations.

In addition, we remeasured the bolivar denominated monetary accounts in its wholly owned subsidiaries at the SICAD 2 rate as it was determined that this exchange mechanism is applicable to these subsidiaries. This resulted in the recognition of a \$2 million loss in the second quarter of fiscal 2014, which was recorded within Other (expense) income within the Consolidated Statements of Operations. We also recognized a tax benefit of \$2 million from a reduction in its bolivar denominated deferred tax liability due to the impact of the devaluation of the bolivar on unremitted earnings.

From a segment reporting perspective, the net impact of the devaluation to our Consolidated Statements of Operations was \$1 million in the second quarter of fiscal 2014.

The operating entity has been profitable historically and has significant export operations from which it is entitled to retain a certain percentage of the foreign currency that it collects, which is principally the U.S. dollar. We continue to closely monitor developments in Venezuela and their potential impact on the recoverability of our equity affiliate investment.

We closely monitor our ability to convert our bolivar holdings into U.S. dollars, as we intend to convert substantially all bolivars held by our wholly owned subsidiaries in Venezuela to U.S. dollars as soon as practical. Any future change in the SICAD 2 rate or opening of additional parallel markets could lead us to change the exchange rate we use and result in gains or losses on the bolivar denominated assets held by its wholly owned subsidiaries.

Purchase Commitments

Cabot has entered into long-term purchase agreements primarily for the purchase of raw materials. Under certain of these agreements the quantity of material being purchased is fixed, but the price paid changes as market prices change. For those commitments, the amounts included in the table below are based on market prices at March 31, 2014.

| | Payments Due by Fiscal Year | | | | | | Total |
|-------------------------|-----------------------------|--------------|--------------|--------------|--------------|-----------------|----------------|
| | Remainder of Fiscal 2014 | 2015 | 2016 | 2017 | 2018 | Thereafter | |
| | (Dollars in millions) | | | | | | |
| Reinforcement Materials | \$ 202 | \$321 | \$ 300 | \$186 | \$178 | \$ 2,795 | \$3,982 |
| Performance Materials | 23 | 39 | 33 | 30 | 30 | 236 | 391 |
| Advanced Technologies | 1 | 2 | 1 | 1 | 1 | — | 6 |
| Purification Solutions | 15 | 16 | 9 | 9 | 9 | 16 | 74 |
| Total | \$ 241 | \$378 | \$343 | \$226 | \$218 | \$ 3,047 | \$4,453 |

Off-balance sheet arrangements

Cabot has no material transactions that meet the definition of an off-balance sheet arrangement.

Forward-Looking Information

This report on Form 10-Q contains “forward-looking statements” under the Federal securities laws. These forward-looking statements address expectations or projections about the future, including the amount and timing of the charge to earnings we will record and the cash outlays we will make in connection with the closing of certain manufacturing facilities and restructuring initiatives; our estimated future amortization expenses for our intangible assets; the sufficiency of our cash on hand, cash provided from operations and cash available under our credit facilities to fund our cash requirements; uses of available cash including anticipated capital spending and future cash outlays associated with long-term contractual obligations; our expected tax rate for fiscal 2014; the recoverability of our equity affiliate investment in Venezuela; and the possible outcome of legal and environmental proceedings. From time to time, we also provide forward-looking statements in other materials we release to the public and in oral statements made by authorized officers.

Forward-looking statements are based on our current expectations, assumptions, estimates and projections about Cabot’s businesses and strategies, market trends and conditions, economic conditions and other factors. These statements are not guarantees of future performance and are subject to risks, uncertainties, potentially inaccurate assumptions, and other factors, some of which are beyond our control or difficult to predict. If known or unknown risks materialize, or should underlying assumptions prove inaccurate, our actual results could differ materially from those expressed in the forward-looking statements.

In addition to factors described elsewhere in this report, the following are some of the factors that could cause our actual results to differ materially from those expressed in the forward-looking statements: changes in raw material costs; lower than expected demand for our products; the loss of one or more of our important customers; our inability to complete capacity expansions or other development projects, including at our mine in Manitoba, as planned; the timing of implementation of environmental regulations; the availability of raw materials; our failure to develop new products or to keep pace with technological developments; fluctuations in currency exchange rates; patent rights of others; stock and credit market conditions; the timely commercialization of products under development (which may be disrupted or delayed by technical difficulties, market acceptance, competitors’ new products, as well as difficulties in moving from the experimental stage to the production stage); demand for our customers’ products; competitors’ reactions to market conditions; delays in the successful integration of structural changes, including acquisitions or joint ventures; severe weather events that cause business interruptions, including plant and power outages or disruptions in supplier or customer operations; the accuracy of the assumptions we used in establishing reserves for environmental matters and for our share of liability for respirator claims; and the outcome of pending litigation. Other factors and risks are discussed in our 2013 10-K.

Recently Issued Accounting Pronouncements – Not Yet Adopted

In July 2013, the FASB issued a new standard related to the “Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists”. The standard requires, unless certain conditions exist, an unrecognized tax benefit or a portion of an unrecognized tax benefit be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, similar to a tax loss or a tax credit carryforward. This standard is applicable for fiscal years beginning after December 15, 2013, and for interim periods within those years. Accordingly, we will adopt this standard beginning October 1, 2014, in the beginning of the first quarter of our 2015 fiscal year. We are currently evaluating the impact of the adoption of this standard on our consolidated financial statements and we do not expect the impact to be material.

In April 2014, the FASB issued a new standard related to the “Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity”. The standard requires discontinued operations treatment for disposals of a component or group of components that represents a strategic shift that has or will have a major impact on an entity’s operations or financial results and requires additional disclosures for discontinued operations and new disclosures for individually material disposal transactions that do not meet the definition of a discontinued operation. This standard is applicable for fiscal years beginning after December 15, 2014 and for interim periods within those years with early adoption permitted but only for disposals that have not been reported in financial statements previously issued. Accordingly, we expect to adopt this standard beginning October 1, 2015, the beginning of the first quarter of our 2016 fiscal year. The impact of the adoption of this standard may have a material impact on our consolidated financial statements based on the nature of the future disposals.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Information about market risks for the period ended March 31, 2014 does not differ materially from that discussed under Item 7A of our 2013 10-K.

Item 4. Controls and Procedures

As of March 31, 2014, we carried out an evaluation, under the supervision and with the participation of our management, including our President and Chief Executive Officer and our Executive Vice President and Chief Financial Officer, of the effectiveness of our disclosure controls and procedures pursuant to Rule 13a-15 under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Based upon that evaluation, our President and Chief Executive Officer and our Executive Vice President and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of that date.

There were no changes in our internal control over financial reporting that occurred during our fiscal quarter ended March 31, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Part II. Other Information

Item I. Legal Proceedings

Respirator Liabilities

We have exposure in connection with a safety respiratory products business that a subsidiary acquired from American Optical Corporation ("AO") in an April 1990 asset purchase transaction. The subsidiary manufactured respirators under the AO brand and disposed of that business in July 1995. In connection with its acquisition of the business, the subsidiary agreed, in certain circumstances, to assume a portion of AO's liabilities, including costs of legal fees together with amounts paid in settlements and judgments, allocable to AO respiratory products used prior to the 1990 purchase by the Cabot subsidiary. As more fully described in our 2013 10-K, the respirator liabilities involve claims for personal injury, including asbestosis, silicosis and coal worker's pneumoconiosis, allegedly resulting from the use of respirators that are alleged to have been negligently designed or labeled.

As of March 31, 2014 and September 30, 2013, there were approximately 41,000 and 42,000 claimants, respectively, in pending cases asserting claims against AO in connection with respiratory products. We have a reserve to cover our expected share of liability for existing and future respirator liability claims. At March 31, 2014 and September 30, 2013, the reserve was \$9 million and \$11 million, respectively, on a discounted basis (\$13 million and \$15 million on an undiscounted basis at March 31, 2014 and September 30, 2013, respectively). The reserve is being accreted up to the undiscounted liability through interest expense over the expected cash flow period, which is through 2065. Cash payments related to this liability were \$2 million and \$1 million in the first six months of fiscal 2014 and 2013, respectively.

Other Matters

We are subject to various other lawsuits, claims and contingent liabilities. In our opinion, although final disposition of some or all of these other suits and claims may impact our consolidated financial statements in a particular period, they should not, in the aggregate, have a material adverse effect on our financial position.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The table below sets forth information regarding Cabot's purchases of its equity securities during the quarter ended March 31, 2014:

Issuer Purchases of Equity Securities

| Period | Total Number of Shares Purchased⁽¹⁾ | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs⁽¹⁾ | Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs⁽¹⁾ |
|--------------------------------------|---|-------------------------------------|---|---|
| January 1, 2014 - January 31, 2014 | — | \$ — | — | 1,636,167 |
| February 1, 2014 - February 28, 2014 | — | \$ — | — | 1,636,167 |
| March 1, 2014 - March 31, 2014 | 379 | \$ 54.73 | 379 | 1,635,788 |
| Total | 379 | | 379 | |

(1) On May 11, 2007, we publicly announced that the Board of Directors authorized us to repurchase five million shares of our common stock on the open market or in privately negotiated transactions. On September 14, 2007, the Board of Directors increased the share repurchase authorization to 10 million shares (the "2007 Authorization"). This authorization does not have a set expiration date. In the second quarter of fiscal 2014 we repurchased 379 shares under this authorization.

[Table of Contents](#)

Item 6. Exhibits

The following Exhibits are filed herewith:

| <u>Exhibit No.</u> | <u>Description</u> |
|------------------------|---|
| Exhibit 31.1* | Certification of Principal Executive Officer required by Rule 13a-14(a) or Rule 15d-14(a) of the Exchange Act. |
| Exhibit 31.2* | Certification of Principal Financial Officer required by Rule 13a-14(a) or Rule 15d-14(a) of the Exchange Act. |
| Exhibit 32** | Certifications of the Principal Executive Officer and the Principal Financial Officer pursuant to 18 U.S.C. Section 1350. |
| Exhibit 101.INS* | XBRL Instance Document. |
| Exhibit 101.SCH* | XBRL Taxonomy Extension Schema Document. |
| Exhibit 101.CAL* | XBRL Taxonomy Calculation Linkbase Document. |
| Exhibit 101.DEF* | XBRL Taxonomy Extension Definition Linkbase Document. |
| Exhibit 101.LAB* | XBRL Taxonomy Label Linkbase Document. |
| Exhibit 101.PRE* | XBRL Taxonomy Presentation Linkbase Document. |

* Filed herewith.

** Furnished herewith.

Attached as Exhibit 101 to this report are the following documents formatted in XBRL (Extensible Business Reporting Language): (i) the Consolidated Statements of Operations for the three and six months ended March 31, 2014 and 2013; (ii) the Consolidated Statements of Comprehensive Income (Loss) for the three and six months ended March 31, 2014 and 2013; (iii) the Consolidated Balance Sheets at March 31, 2014 and September 30, 2013; (iv) the Consolidated Statements of Cash Flows for the six months ended March 31, 2014 and 2013; and (v) Notes to Consolidated Financial Statements, March 31, 2014.

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.

CABOT CORPORATION

Date: May 7, 2014

By: /s/ EDUARDO E. CORDEIRO

Eduardo E. Cordeiro
Executive Vice President and Chief Financial Officer
(Duly Authorized Officer)

Date: May 7, 2014

By: /s/ JAMES P. KELLY

James P. Kelly
Vice President and Controller
(Chief Accounting Officer)

Exhibit Index

| <u>Exhibit No.</u> | <u>Description</u> |
|--------------------|---|
| Exhibit 31.1* | Certification of Principal Executive Officer required by Rule 13a-14(a) or Rule 15d-14(a) of the Exchange Act. |
| Exhibit 31.2* | Certification of Principal Financial Officer required by Rule 13a-14(a) or Rule 15d-14(a) of the Exchange Act. |
| Exhibit 32** | Certifications of the Principal Executive Officer and the Principal Financial Officer pursuant to 18 U.S.C. Section 1350. |
| Exhibit 101.INS* | XBRL Instance Document. |
| Exhibit 101.SCH* | XBRL Taxonomy Extension Schema Document. |
| Exhibit 101.CAL* | XBRL Taxonomy Calculation Linkbase Document. |
| Exhibit 101.DEF* | XBRL Taxonomy Extension Definition Linkbase Document. |
| Exhibit 101.LAB* | XBRL Taxonomy Label Linkbase Document. |
| Exhibit 101.PRE* | XBRL Taxonomy Presentation Linkbase Document. |

* Filed herewith.

** Furnished herewith.

Attached as Exhibit 101 to this report are the following documents formatted in XBRL (Extensible Business Reporting Language): (i) the Consolidated Statements of Operations for the three and six months ended March 31, 2014 and 2013; (ii) the Consolidated Statements of Comprehensive Income (Loss) for the three and six months ended March 31, 2014 and 2013; (iii) the Consolidated Balance Sheets at March 31, 2014 and September 30, 2013; (iv) the Consolidated Statements of Cash Flows for the six months ended March 31, 2014 and 2013; and (v) Notes to Consolidated Financial Statements, March 31, 2014.

Principal Executive Officer Certification

I, Patrick M. Prevost, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Cabot Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 7, 2014

/s/ PATRICK M. PREVOST

Patrick M. Prevost

President and Chief Executive Officer

Principal Financial Officer Certification

I, Eduardo E. Cordeiro, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Cabot Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 7, 2014

/s/ EDUARDO E. CORDEIRO

Eduardo E. Cordeiro

Executive Vice President and Chief Financial Officer

**Certifications Pursuant to 18 U.S.C. Section 1350,
as Adopted Pursuant to Section 906 of the
Sarbanes-Oxley Act of 2002**

In connection with the filing of the Quarterly Report on Form 10-Q for the quarter ended March 31, 2014 (the "Report") by Cabot Corporation (the "Company"), each of the undersigned hereby certifies pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to his knowledge:

1. The Report fully complies with the requirements of section 13 (a) or 15 (d) of the Securities Exchange Act of 1934, as amended; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/S/ PATRICK M. PREVOST

Patrick M. Prevost
President and Chief Executive Officer
May 7, 2014

/S/ EDUARDO E. CORDEIRO

Eduardo E. Cordeiro
*Executive Vice President and
Chief Financial Officer*
May 7, 2014

