

A Schulman, Inc. SHLM (NAS)

| Last Close | Industry | Sector |
|------------|-------------------|----------------|
| 17.45 USD | Rubber & Plastics | Consumer Goods |

Profile

Pricing data through 19 Nov 2009

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A. Schulman, Inc. ("A. Schulman,") was organized as an Ohio corporation in 1928 and changed its state of incorporation to Delaware in 1969. It is an international supplier of high-performance plastic compounds and resins. A. Schulman is a global plastics compounder, specializing in multi-component blends that include polyolefins, nylons, elastomers, ionomers and ABS (acrylonitrile butadiene styrene). A. Schulman operates three lines of business: engineered plastics, masterbatch and distribution services. The Company's segments are Europe, North America Masterbatch ("NAMB") (previously, referred to as North America Polybatch or NAPB), North America Engineered Plastics ("NAEP"), North America Distribution Services ("NADS") (which includes rotomolding) and Asia. Its activities in each of its business segments could be classified into five main product families: color and additive concentrates; engineered compounds; polyolefins; PVC; and tolling. The Company's color and additive concentrates business consists of the compounding of resins that provide plastic with specific color and/or physical properties, such as conductivity, flexibility, viscosity and textures. Its engineered compounds are products designed to have and maintain characteristics such as chemical resistance, electrical conductivity, heat resistance and/or high strength-to-weight ratios. The Company's polyolefin business consists of numerous polypropylene and polyethylene resins and compounds. The Company's PVC business, under the name Polyvin (r), involves the formulation of compounds and elastomers to introduce product attributes, including weatherability, consistency, ease of processing, material flexibility, and high-gloss or low-gloss finish. The Company provides tolling services, mainly in Europe, as a fee for processing of material provided and owned by customers. The research and development centers are in Sindorf, Germany and Akron, Ohio. The Company competes with producers of basic plastic resins, many of which also operate compounding plants, as well as other independent plastic compounders. Its operations on and ownership of real property are subject to environmental, health and safety laws and regulations at the national, state and local governmental levels.

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Management & Ownership

Management Activity

| Name | Position | Shares Held | Report Date* | InsiderActivity |
|---------------------|---|-------------|--------------|-----------------|
| ANDRES RONALD G | Vice President | 60,763 | 11 Apr 2008 | - |
| TAYLOR JACK B | General Manager | 60,000 | 23 Oct 2009 | - |
| GINGO JOSEPH M | Chief Executive Officer, Director | 39,600 | 16 Jan 2009 | - |
| DESANTIS PAUL F | Chief Financial Officer, Vice President | 30,887 | 11 Apr 2009 | - |
| CURD HOWARD R | Director | 10,500 | 13 May 2008 | - |
| MINC DAVID C. | General Counsel, Vice President | 9,447 | 24 Jun 2009 | - |
| MILLER GARY A | CPO, Vice President | 9,337 | 04 Jun 2009 | - |
| MITAROTONDA JAMES A | Director | 7,000 | 24 Jul 2009 | - |
| CAPORALE MICHAEL JR | Director | 6,000 | 27 May 2009 | - |

*Report date represents the date on which the owner's common shares held was audited.

Fund Ownership

| Top Owners | Morningstar Rating | % of Shares Held | % of Fund Assets | Change (k) | Portfolio Date |
|--------------------------------------|--------------------|------------------|------------------|------------|----------------|
| DFA US Small Cap Value I | QQQ | 2.70 | 0.22 | -62 | 30 Jun 2009 |
| Royce Low Priced Stock Svc | QQQQ | 2.20 | 0.32 | -50 | 30 Jun 2009 |
| Evergreen Special Values A | QQQ | 2.06 | 0.84 | -17 | 30 Jun 2009 |
| Royce Special Equity Invmt | QQQQQ | 1.51 | 0.74 | 96 | 30 Jun 2009 |
| Vanguard Small Cap Index | QQQ | 1.12 | 0.05 | 6 | 31 Jul 2009 |
| Concentrated Holders | | | | | |
| Virtus Disciplined Small Cap Value I | QQQ | 0.33 | 1.15 | 13 | 30 Jun 2009 |
| Victory Small Company Opportunity R | QQQQ | 0.94 | 1.03 | 39 | 30 Jun 2009 |

Institutional Transactions

| Top 5 Buyers | Morningstar Rating | % of Shares Held | % of Fund Assets | Shares Bought/Sold (k) | Portfolio Date |
|--------------------------------------|--------------------|------------------|------------------|------------------------|----------------|
| Royce Special Equity Invmt | QQQQQ | 1.51 | 0.74 | 96 | 30 Jun 2009 |
| Forward Small Cap Equity | QQQ | 0.33 | 0.47 | 86 | 31 Jul 2009 |
| American Century Small Cap Value Inv | QQQQQ | 0.69 | 0.24 | 85 | 30 Jun 2009 |
| Vanguard Global Equity | QQQ | 0.32 | 0.05 | 78 | 30 Jun 2009 |
| Northern Small Cap Value | QQQ | 0.87 | 0.30 | 68 | 30 Jun 2009 |
| Top 5 Sellers | | | | | |
| DFA US Small Cap Value I | QQQ | 2.70 | 0.22 | -62 | 30 Jun 2009 |
| Royce Low Priced Stock Svc | QQQQ | 2.20 | 0.32 | -50 | 30 Jun 2009 |
| Evergreen Special Values A | QQQ | 2.06 | 0.84 | -17 | 30 Jun 2009 |
| Oppenheimer Main St Opportunity A | QQ | 0.07 | 0.02 | -17 | 30 Apr 2009 |

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Industry Focus: Auto Parts Manufacturing

David Manger
 Associate Analyst

Despite the Detroit Three's struggles, some auto suppliers remain well positioned.

Sorting Out the Wreckage among Auto Suppliers 29 June 2009

Automotive suppliers of both high and low quality enjoyed the early part of the decade, when automotive original-equipment manufacturers thrived on profitable light trucks and SUVs. With the belief that record sales volumes of nearly 17 million vehicles were sustainable, the automotive manufacturing base exploded.

However, when the credit crisis struck in the fall of 2008, vehicle sales plummeted. In response, OEMs slashed production at unprecedented rates in an attempt to combat expanding inventories. Adding to the problems, General Motors GMGMQ and Chrysler extended scheduled plant shutdowns as they entered bankruptcy, depriving many North American suppliers of their main revenue sources. Reflective of these challenges, three Tier 1 suppliers (firms that supply OEMs)--Hayes-Lemmerz HAYZQ, Metaldyne, and Visteon VSTN --along with numerous smaller suppliers recently filed for bankruptcy. With much of the supplier network coping with severe financial distress, the outlook for the industry as a whole may appear dim, but we'll highlight several firms we think are positioned to emerge

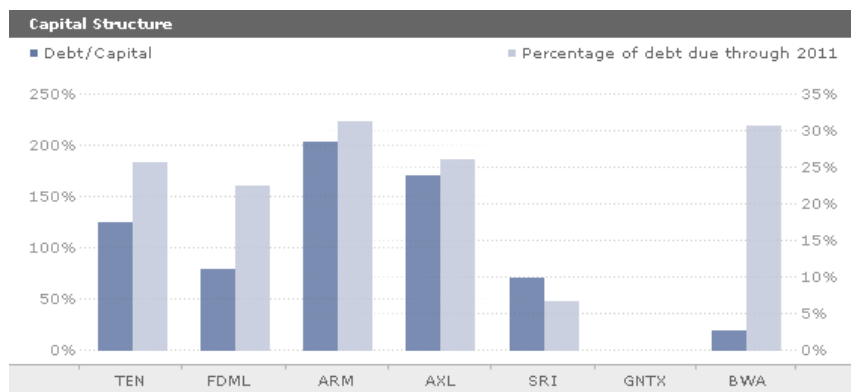
from the downturn on top.

Reacting to a New Reality

Last year, domestic light-vehicle sales fell to approximately 13.2 million units, down nearly 24% from an all-time high of around 17.3 million units in 2000. Now, vehicle sales are on pace to reach 10 million units, levels not seen since the early 1980s. This dramatic production decline has crushed profitability at both automakers and suppliers, which operate under highly fixed cost structures. Suppliers' responses have included nearly every cost-cutting tool imaginable. For instance, American Axle AXL plans to lay off an additional 25% of its workforce after slashing around 70% of its domestic capacity and more than 25% of its workforce in 2008. Highlighting the rapid pace of the downturn, in mid-2008 Axle's restructuring plans targeted break-even levels at annual domestic sales of 13 million-14 million units. Now the firm and many other suppliers are working toward break-even levels closer to 10 million units. Other suppliers undertaking aggressive restructuring programs include Federal-Mogul FDML, which cut 20% of its workforce, Tenneco TEN (cut 10%), ArvinMeritor ARM (cut 15%), BorgWarner BWA (cut 24%), and Gentex GNTX (cut 16%). Aside from workforce reductions, many suppliers have suspended 401(k) programs, reduced workweeks, froze salaries, implemented employee furloughs, and cut executive pay.

Looming Liquidity Crisis

If the unprecedented decline in production wasn't enough of a blow to suppliers, the inability to gain access to affordable credit may be the knockout punch. The billing cycle in the auto industry usually ranges from 45 to 60 days. Therefore, suppliers fund raw-material and payroll expenses for anticipated demand with cash reserves or bank loans. Given the distress in the auto industry, many financial institutions have begun reducing their exposure to auto-related firms, limiting suppliers' access to capital. Making matters worse, as losses mount, suppliers have been burning through cash at alarming rates. In the first quarter alone, American Axle's cash reserves declined more than



Source: Company Filings, Morningstar Research

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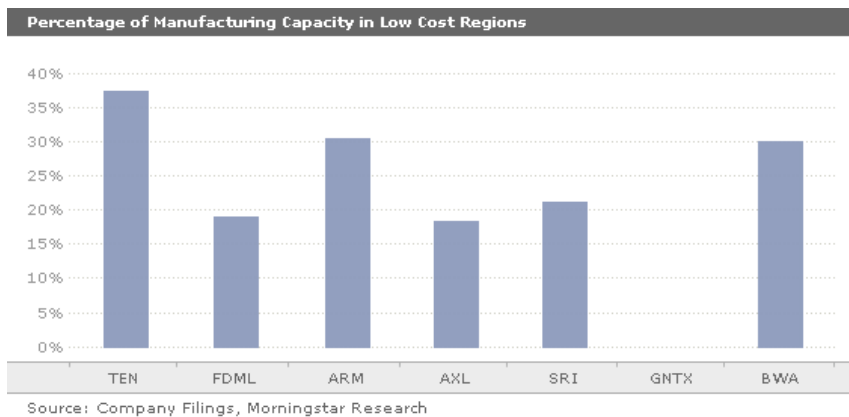
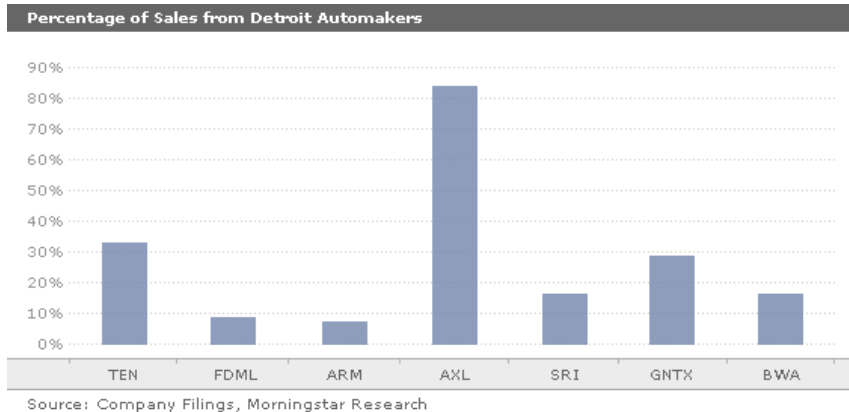
\$60 million, while Tenneco and BorgWarner each experienced declines of nearly \$13 million.

Currently, we don't believe any of the suppliers mentioned in this article are in danger of running out of cash, but a prolonged production decline could jeopardize this assumption, especially for American Axle. Greater concern lies with smaller suppliers that sell to Tier 1 firms. We think these companies will likely struggle to meet working-capital needs when production rebounds, which could prove problematic for the firms we cover, given the time and resources required to switch suppliers. This was evident in

the first quarter when several Tier 1 suppliers provided financial assistance and renegotiated contracts with cash-strapped suppliers. Having recently been denied \$8 billion-\$10 billion in government aid, these smaller financially distressed suppliers pose major supply-chain risks for the entire auto industry.

The Balance Sheet Effects of a Period Defined by Cheap Credit

During the height of the credit bubble in 2007, many suppliers aggressively expanded production capacity by leveraging their balance sheets. At the time, it didn't seem like a bad idea because demand was strong and capital was available at attractive rates. However, it appears little thought was given to the possibility of managing the massive debt burdens at current demand levels. Nowhere is this more evident than American Axle, Tenneco, and Arvin Meritor, which all have debt/capital ratios north of 120% (a negative book equity resulting from significant losses contributes to ratios in excess of 100%). On the other hand, Gentex has a pristine balance sheet, featuring no debt and respectable cash reserves. We also rank BorgWarner's balance sheet in the top tier of auto suppliers, given its debt/capital ratio of approximately 20%.



Despite the unattractive debt/capital ratios at American Axle and Tenneco, only around 26% of each firm's total obligations are due before 2011. By this time, we think vehicle sales will have rebounded from their lows, allowing for higher profits capable of supporting the debt maturities. We also believe Stoneridge's SRI minimal obligations coming due will allow it to remain nimble in its pursuit of growth.

Penetrating New Markets to Diversify From Big Three

For years, suppliers have tried to diversify their revenues from light-vehicle markets, especially relationships with the Detroit automakers (Ford, GM, and Chrysler). Compared

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with commercial vehicles, light-vehicle markets are typically more fragmented at the OEM level. These OEMs constantly pressure suppliers to accept price concessions, resulting in greater price competition and reduced profitability. This is magnified when OEMs encounter financial distress, leaving little opportunity for profits at suppliers. In recent years, few firms have encountered more financial struggles than the Detroit automakers. It's easy to see American Axle has failed to dodge this oncoming freight train, as adjusted operating margins declined to negative 3% in 2008 from nearly 9% in 2000. Of the suppliers mentioned in this article, Gentex and Tenneco also generate a large chunk of their revenue from the distressed automakers, though far less than Axle.

Conversely, diversification efforts by Federal-Mogul and ArvinMeritor have been impressive. We're especially encouraged by Federal-Mogul's customer base, with no individual customer accounting for more than 5% of sales and over 50% of revenue derived internationally. Similarly, ArvinMeritor's diversification stems from its penetration into commercial vehicle markets, which account for roughly 70% of total sales. Not only do these markets offer less pricing pressure from customers, but they also have greater economies of scale--a production facility for commercial-vehicle parts accounts for a much larger percentage of global capacity than an equivalent light-vehicle facility.

Historically, foreign OEMs have favored foreign suppliers, limiting global diversification opportunities for firms based in North America. Nevertheless, we see this process changing as suppliers develop relationships with foreign OEMs through joint ventures and establish manufacturing facilities in low-cost regions. Here, Tenneco appears ahead of the curve, with around 37% of its manufacturing capacity in low-cost regions. As evidence of this advantage, the firm recently expanded its position as a leading emission control supplier in China with a joint venture to supply parts for Beijing Hyundai. We also think ArvinMeritor and

BorgWarner are capable of attracting foreign customers through their global footprints.

Potential Profits for Suppliers

Despite slack in domestic vehicle sales, an aging vehicle fleet and possible government-sponsored programs designed to encourage new vehicle purchases are likely to increase demand, though we don't expect them to reach the levels achieved in 2000. From an international standpoint, growth appears more promising, especially in China, India, and Brazil. Moreover, we think some suppliers will have the opportunity to generate respectable margins, given drastically lower break-even levels and industry consolidation. We believe one of the main drivers behind the consolidation will be increased collaboration between OEMs and suppliers. Lately, automakers have designed several vehicle models based on a single platform, limiting the amount of parts necessary for multiple models. We think this process will require fewer suppliers, with reduced price competition as a result.

During the last month, stock prices of many suppliers have climbed substantially, as it became apparent the government would not let GM or Chrysler liquidate. Still, we believe Gentex, BorgWarner, Stoneridge, and Tenneco are some of the suppliers worth keeping on your radar.

Stoneridge SRI Stoneridge is a niche supplier of electrical components to commercial- and light-vehicle markets. The firm's biggest driver is its profitable Brazilian joint venture, PST Eletronica. The joint venture's dominant market share for automotive accessories in the emerging Brazilian market should fuel future growth.

Gentex GNTX With more than 400 patents worldwide and a dominant 83% market share for auto-dimming rearview and side mirrors, Gentex is one of the few auto suppliers that has carved a narrow economic moat. We expect growth to be driven by the firm's commitment to

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investing in research and development. A debt-free balance sheet also provides flexibility in pursuing future opportunities.

BorgWarner BWA Implementation of increased fuel-efficiency and emissions standards should benefit BorgWarner. The firm's product portfolio is filled with solutions designed to help vehicles meet stringent regulations. Specifically, we think the firm's turbocharger and transmission products will be a major growth driver.

Tenneco TEN Tenneco should also benefit from tighter emission standards and a growing market for diesel vehicles through its diesel exhaust filters. We think growth will be supported by a market-leading position in the supply of emission-control products in the rapidly growing Chinese market.