ANNUAL REPORT

NATIONAL GYPSUM COMPANY

DECEMBER 31, 1939
DIRECTORS

MELVIN H. BAKER          EDWIN F. GUTH
RALPH F. BURLEY          WILLIAM G. HOUCK
WILLIAM M. CURRIE       JOSEPH A. W. IGLEHART
ELMER E. FINCK          GORDON H. TARBELL

OFFICERS

MELVIN H. BAKER . . . . . . . . PRESIDENT
RALPH F. BURLEY . . . . . . . . VICE PRESIDENT
GORDON H. TARBELL . . . . . . VICE PRESIDENT
JOHN C. BEST . . . . . . . . VICE PRESIDENT
FRANK E. DAVIS . . SECRETARY AND TREASURER
WALTER S. CORRIE . . . . . . CONTROLLER
CHARLES E. MASTERS . . ASSISTANT TREASURER
ROBERT O. WILLIAMS . . ASSISTANT SECRETARY

TRANSFER AGENTS

BANKERS TRUST COMPANY—NEW YORK, N. Y.
The Marine Midland Trust Company of New York
NEW YORK, N. Y.

REGISTRARS

THE MARINE MIDLAND TRUST COMPANY OF NEW YORK
NEW YORK, N. Y.
MANUFACTURERS TRUST COMPANY—NEW YORK, N. Y.
To the Stockholders of
National Gypsum Company:

This report covers your Company's operations for the year ended December 31, 1939.

Earnings for that period were $1,455,237 as compared with $921,632 for 1938. These were net after allowances for Federal and Dominion taxes, and Canadian exchange adjustment. Business improved as the year went along and 53% of earnings for the year were made in the last six months.

Income for the year was equal to 94¢ per share on the Common stock, to compare with 49¢ per share earned in 1938.

Sales likewise showed substantial increase, running 32% over 1938. Increased volume and careful attention to operating economies accounted for the improvement in earnings.

Taxes again increased. Direct taxes included in operating costs and those deducted from income amounted to $544,623, an increase of $137,374 over the previous year. Taxes for the year were equivalent to 43¢ per share on the Common stock.

The Balance Sheet on following pages shows current assets of $6,511,280 and current liabilities of $1,329,025. This compares with current assets of $6,483,405 and current liabilities of $929,982 for 1938. Total assets of $18,876,269 were $2,505,892 greater than a year ago.

In addition to the regular dividends of $270,008 on the Preferred stock, a dividend amounting to $315,365 was paid on the Common stock. After deducting cost of financing and Canadian exchange adjustment, earned surplus was $1,291,200 to compare with $686,333 at the close of 1938.
The Company's 4¾% bonds were refunded by a $5,000,000 issue of fifteen-year 3¾% Debentures. By this action not only was the rate of interest reduced, but new capital obtained at an exceptionally low rate.

Of the stock set aside for sale to employees there were 77,532 shares remaining to be issued over the next four years. A price of $10 per share has been fixed on 25% of these shares that may be taken up on December 20, 1940. As provided for in the employee stock plan, price for the remaining shares will be fixed by the Board of Directors in January of each year thereafter.

Earnings for the year benefited substantially from recently acquired units. The insulation board plant at Mobile, Alabama, produced in this, its first full year of operation, a net profit equal to about 10% on capital there invested.

The new gypsum plant at Savannah, Georgia, went into production in May and showed a profit for each month thereafter. Based on the number of new dealers secured in the South last year, increased production can be expected at Savannah for 1940.

The Canadian Government completed last Fall a new harbor at Dingwall, Nova Scotia, permitting the use of 8,000-ton instead of 2,000-ton ships. The first of these unloaded at Savannah in December. During 1940 the Company will benefit from the use of larger ships in handling and transporting gypsum to its plants at Portsmouth, Savannah and New York City.

Best Bros. Keene's Cement Company's property purchased in 1938 continued to prove a profitable acquisition. The large facilities in this unit at Medicine Lodge, Kansas, will be utilized to manufacture certain new products now in development without interfering with present production.

The new board plant and other important additions to the New York property will be finished in time for Spring business. When completed this operation will place the Company in a strong position to increase sales and improve its profit in the metropolitan market.

The Company now markets a line of 141 products through lumber and building material dealers. These products are designed for interior construction of all types of walls and ceilings. Each is a logical part of the original plan for a complete line of closely related products to be distributed through one class of trade.
Gypsum and lime products are heavy and sold at low prices, so freight is an important factor in determining profit. The plant expansion program of the past has been an endeavor to locate near the principal markets as a logical means for reducing transportation charges. Increased earnings from year to year have demonstrated the wisdom of this policy.

From the very beginning research has been vital to the Company's leadership in product quality, in pioneering new materials, and in developing new uses. In furtherance of this policy a new laboratory building has been opened at Clarence Center, New York, fully equipped and staffed for more extensive research work.

Continuity of management personnel has been a major factor in the growth of the Company over the past fourteen years. Most of the present Directors were on the original Board. Senior and junior executives, plant managers and department heads have risen from the ranks. Thus, the organization has benefited from cumulative experience essential to perpetuation of those policies responsible for profitable operations.

This organization with its intelligence, loyalty and enthusiasm deserves recognition for making possible this report of progress.

The situation in the building field during the past year may have been confusing to many stockholders. Activity increased sharply and there was much publicity about Government financing, low-cost housing, labor costs, prices, and revolutionary changes in construction.

Because of this confusion it was felt that stockholders would find the enclosed booklet interesting and informative. It covers important developments during the year and describes the Company's position in the building field.

Respectfully yours,

[Signature]

President
CONSOLIDATED BAI
NATIONAL GYPSUM COMPANY
December 31,

ASSETS

CURRENT
Cash funds and demand deposits $1,517,066.11
Time deposits, including interest 573,560.87 $2,090,626.98
Notes, acceptances and accounts receivable, trade ($185,076.98 reserve deducted) 2,008,285.82
Inventories—at lower of cost or market:
Products finished and in process $1,319,160.03
Materials and supplies 1,093,206.67 $2,412,366.70
Less reserves for depletion 132,054.09 $2,080,312.61
Plant sites
Buildings, docks, machinery and equipment $9,868,835.41
Less reserves for depreciation 1,627,115.93 8,241,719.48
Construction in process (Note B)
Idle plant 1,144,855.96
Inventories of repair parts, etc. 125,129.70 502,964.01
Bond discount and expense (unamortized balance)

INVESTMENTS AND OTHER ASSETS
Capital stock of inactive subsidiary not consolidated $ 1,000.00
Employee loans, accounts and travel advances 63,372.10
Miscellaneous accounts receivable, investments, claims, etc. ($19,068.06 reserves deducted) 48,412.88
Securities (at cost and accrued interest) on deposit with State and Dominion Governments 93,845.43
Real estate not used in operations (including land at $142,668.00 subject to vendor's option to repurchase at same price)—at cost, less $50,000.00 reserve for loss on property sold in January, 1940 190,171.33 396,801.74

PROPERTY, PLANTS AND EQUIPMENT (Note A)
Mineral deposits and timberland:
Owned gypsum and lime deposits $ 947,725.45
Leased gypsum and lime deposits 574,887.94
Owned timberland 31,031.20
Less reserves for depletion 132,054.09 1,421,590.50

Plant sites 589,113.50
Buildings, docks, machinery and equipment $9,868,835.41
Less reserves for depreciation 1,627,115.93 8,241,719.48
Construction in process (Note B)
Idle plant 1,144,855.96
Inventories of repair parts, etc. 125,129.70 502,964.01
Bond discount and expense (unamortized balance)

PATENTS, TRADE-MARKS AND COPYRIGHTS
Cost less amortization 67,943.04

DEFERRED CHARGES
Unexpired insurance premiums, prepaid taxes, royalties, etc. $197,022.59
Improvements to leased property (unamortized balance) 12,777.15
Inventories of repair parts, etc. 168,034.57
Bond discount and expense (unamortized balance)

$18,876,268.73

Principles of consolidation and the notes refer...
## BALANCE SHEET
**COMPANY AND SUBSIDIARY**

### 31, 1939

### LIABILITIES

#### CURRENT

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accounts payable, trade and sundry</td>
<td>$663,005.71</td>
</tr>
<tr>
<td>Federal capital stock, state franchise and local property taxes</td>
<td>42,476.74</td>
</tr>
<tr>
<td>Federal and state pay roll taxes</td>
<td>51,914.92</td>
</tr>
<tr>
<td>Accrued interest, insurance and royalties</td>
<td>104,974.45</td>
</tr>
<tr>
<td>Federal (U. S. and Canada), state and provincial taxes on income—estimated</td>
<td>271,652.69</td>
</tr>
<tr>
<td>3% Sinking Fund Debentures required to be retired in 1940</td>
<td>195,000.00</td>
</tr>
</tbody>
</table>

### 3\% SINKING FUND DEBENTURES (due September 1, 1954)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Authorized and issued</td>
<td>$5,000,000.00</td>
</tr>
<tr>
<td>Less amount included in current liabilities</td>
<td>195,000.00</td>
</tr>
</tbody>
</table>

### RESERVE

For workmen's compensation self-insurance.......................... 42,394.19

### CAPITAL STOCK AND SURPLUS

Capital stock:

- **Cumulative Preferred Stock (without par value):**
  - Authorized—100,000 shares
  - Issued and outstanding — series of $4.50
    - Convertible Cumulative Preferred Stock—60,000 shares at involuntary liquidation price ($100 per share) ................ $6,000,000.00
- **Common Stock ($1 par):**
  - Authorized—2,500,000 shares
  - Reserved for conversion of $4.50 Convertible Cumulative Preferred Stock (on basis of current conversion rate)—305,652 shares
  - Reserved for issuance under Employees' Stock Purchase Plan—77,532 shares
  - Issued and outstanding—1,261,458.03 shares ................ $1,261,458.03

Surplus:

- Capital ........................................... $4,147,192.37
- Earned (from January 1, 1936)—partly restricted as to payment of dividends on Common Stock (Note C) ........................ $12,699,850.03

\[ \text{Total:} \quad \$18,876,268.73 \]

This referred to appear on a following page.
Principles of Consolidation

(a) In accordance with past practice, the accounts of the wholly owned Canadian subsidiary have been consolidated. Withdrawals of investment in and profits of this subsidiary are currently subject to exchange restrictions. Its working assets and current liabilities included in the balance sheet have been translated to a U.S. dollar basis at the rate of exchange at December 31, 1939, the net of the amounts so included being $149,369.28. As in previous years, the accounts for property, plants and equipment ($797,438.64, net) have been included on a dollar for dollar basis. To facilitate comparison with prior years, the operating accounts of the Canadian subsidiary are consolidated on a dollar for dollar basis, less an adjustment of $4,143.81 to bring the net profit of the subsidiary ($41,814.81 Canadian) to the U.S. dollar equivalent at the year end exchange rate.

(b) Subsidiaries which, if consolidated, would have no significant effect on the financial condition and operating accounts of the Company have been excluded from the consolidation.

(c) Transactions between companies consolidated have been eliminated.

Notes to Consolidated Financial Statements

NOTE A: Property, plants and equipment are carried on the basis of cost, less plant and equipment write-down of $1,060,074.01 in 1932. On account of such write-down, depreciation charged against income during 1939 was $46,746.65 less than it would have been if based on original cost.

NOTE B: Construction in process is cost to December 31, 1939. It is estimated that completion of major construction work will require approximately $1,125,000.00. This amount does not include provision for ordinary plant improvements in process or contemplated at December 31, 1939.

NOTE C: Under provisions of the Indenture relating to the 37/8% Sinking Fund Debentures, the balance of surplus at December 31, 1939 available for dividends on the $4.50 Convertible Cumulative Preferred Stock is not limited; the amount available for dividends on Common Stock after December 31, 1939 is restricted to $700,000 plus subsequent net earnings after all dividend and Sinking Fund payments.

LITIGATION: With other litigation of lesser interest there was pending: (a) an action brought by the United States to have declared null and void two gypsum leases with the Tonawanda Nation of Indians and to have declared null and void Section 85 of the Indian Law of the State of New York; (b) an action brought by the Milcor Steel Company against New York City Housing Authority, et al., charging infringement of letters patent relating to wall construction, in which the Company is not a defendant but has indemnified the defendants against any loss because of the use of its materials in a certain Government project; and (c) an action brought by Atlantic Research Associates, Inc., charging infringement of certain patents relating to a particular form of casein interior wall finish. The Company is defending its position in each case.

ACCOUNTANTS' REPORT

We have examined the balance sheet of National Gypsum Company and its subsidiary National Gypsum (Canada) Ltd., as at December 31, 1939, and the statements of profit and loss and surplus for the year then ended, have reviewed the system of internal control and the accounting procedures of the companies and, without making a detailed audit of the transactions, have examined or tested accounting records of the companies and other supporting evidence, by methods and to the extent we deemed appropriate. Receivables were tested by sending statements to debtors requesting that we be notified of any differences, and no important differences were reported to us. We observed the inventory taking at selected locations and dates and satisfied ourselves as to the adequacy of inventory procedures.

In our opinion, the accompanying balance sheet and related statements of profit and loss and surplus present fairly the consolidated position of National Gypsum Company and its consolidated subsidiary at December 31, 1939, and the consolidated results of operations for the year, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

ERNST & ERNST

Buffalo, New York
February 22, 1940