LUBRIZOL CORP
Form 10-Q
November 06, 2003

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2003

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 1-5263

THE LUBRIZOL CORPORATION
(Exact name of registrant as specified in its charter)

Ohio	34-0367600
(State or other jurisdiction of incorporation or organization)	(I.R.S.Employer Identification No.)

29400 Lakeland Boulevard
Wickliffe, Ohio 44092-2298
(Address of principal executive offices)
(Zip Code)

(440) 943-4200
(Registrant's telephone number, including area code)

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 [X]   No [ ]

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes [X] No [ ]

Number of the registrant's common shares, without par value, outstanding, as of September 30, 2003: 51,557,528.

PART I. FINANCIAL INFORMATION
Item 1 Financial Statements

THE LUBRIZOL CORPORATION

CONSOLIDATED BALANCE SHEETS

(In Thousands of Dollars)	September 30, 2003	December 31, 2002
ASSETS		
Cash and short-term investments	$ 215,158	$ 266,428
Receivables	331,015	295,508
Inventories:		
Finished products	153,832	148,478
Products in process	80,194	58,643
Raw materials	80,020	76,779
Supplies and engine test parts	19,727	19,068
	333,773	302,968
Other current assets	39,795	44,875
Total current assets	919,741	909,779
Property and equipment - net	676,554	679,155
Goodwill	205,524	168,352
Intangible assets - net	63,827	43,162
Investments in nonconsolidated companies	6,689	6,690
Other assets	51,088	52,999
TOTAL	$ 1,923,423	$ 1,860,137
LIABILITIES AND SHAREHOLDERS' EQUITY		
Short-term debt and current portion of long-term debt.	$ 11,031	$ 17,046
Accounts payable	149,639	140,424
Accrued expenses and other current liabilities	132,969	150,271
Total current liabilities	293,639	307,741
Long-term debt	382,755	384,845
Postretirement health care obligation	97,935	96,495
Noncurrent liabilities	100,083	92,655
Deferred income taxes	60,024	55,761
Total liabilities	934,436	937,497
Minority interest in consolidated companies	52,792	53,388
Contingencies and commitments		
Shareholders' equity:		
Preferred stock without par value - authorized and unissued:		
Serial Preferred Stock - 2,000,000 shares		
Serial Preference Shares - 25,000,000 shares		
Common shares without par value:		
Authorized 120,000,000 shares		
Outstanding- 51,557,528 shares as of September 30, 2003 after deducting 34,638,366 treasury shares, 51,457,642 shares as of December 31, 2002 after deducting 34,738,252 treasury shares	122,805	118,985
Retained earnings	867,834	828,318
Accumulated other comprehensive loss	(54,444)	(78,051)

Total shareholders' equity	936,195	869,252
TOTAL	$ 1,923,423	$ 1,860,137

Amounts shown are unaudited.
See accompanying notes to the financial statements.

THE LUBRIZOL CORPORATION

CONSOLIDATED STATEMENTS OF INCOME

	Three Month Period Ended September 30		Nine Month Peri Ended September	
(In Thousands Except Per Share Data)	2003	2002	2003	2
Net sales	$ 509,107	$ 509,427	$ 1,530,383	$ 1,
Royalties and other revenues	760	876	2,374	
Total revenues	509,867	510,303	1,532,757	1,
Cost of sales	377,486	358,850	1,118,360	1,
Selling and administrative expenses	48,647	49,530	149,613	
Research, testing and development expenses.	41,022	42,774	123,265	
Restructuring charge	409	-	7,447	
Total cost and expenses	467,564	451,154	1,398,685	1,
Other income (expense) - net	(2,573)	(3,042)	(2,906)	
Interest income	913	1,796	3,015	
Interest expense	(6,611)	(5,791)	(18,669)	
Income before income taxes and cumulative effect of change in accounting principle..	34,032	52,112	115,512	
Provision for income taxes	9,734	15,634	35,808	
Income before cumulative effect of change in accounting principle	24,298	36,478	79,704	
Cumulative effect of change in accounting principle	-	-	-	
Net income	$ 24,298	$ 36,478	$ 79,704	$
Net income per share:				
Income before cumulative effect of change in accounting principle	$ 0.47	$ 0.71	$ 1.54	$
Cumulative effect of change in accounting principle	-	-	-	
Net income per share	$ 0.47	$ 0.71	$ 1.54	$
Net income per share, diluted:				

Income before cumulative effect of change in accounting principle	$ 0.47	$ 0.71	$ 1.54	$
Cumulative effect of change in accounting principle	-	-	-	
Net income per share, diluted	$ 0.47	$ 0.71	$ 1.54	$
Dividends per share	$ 0.26	$ 0.26	$ 0.78	$
Weighted average common shares outstanding.	51,717	51,569	51,680	

Amounts shown are unaudited.
See accompanying notes to the financial statements.

THE LUBRIZOL CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine Month Period Ended September 30	
(In Thousands of Dollars)	2003	2002
Cash provided from (used for):		
Operating activities:		
Net income	$ 79,704	$ 92,997
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation and amortization	74,146	70,898
Deferred income taxes	4,146	(616)
Restructuring charge	3,327	-
Cumulative effect of change in accounting principle	-	7,785
Change in current assets and liabilities:		
Receivables	(18,846)	7,452
Inventories	(13,324)	(13,930)
Accounts payable and accrued expenses	(24,259)	4,712
Other current assets	2,923	(3,215)
Other items - net	5,882	7,069
Total operating activities	113,699	173,152
Investing activities:		
Capital expenditures	(59,485)	(45,976)
Acquisitions and investments in nonconsolidated companies	(67,532)	(69,438)
Other - net	484	2,882
Total investing activities	(126,533)	(112,532)
Financing activities:		
Short-term borrowings(repayments)-net	(6,426)	6,715
Long-term repayments	(227)	(1,654)
Long-term borrowings	15	-
Dividends paid	(40,161)	(40,043)
Proceeds from termination of interest rate swaps	-	18,134

Stock options exercised	3,658	8,203
Total financing activities	(43,141)	(8,645)
Effect of exchange rate changes on cash	4,705	8,485
Net increase (decrease) in cash and short-term investments	(51,270)	60,460
Cash and short-term investments at beginning of period	266,428	189,095
Cash and short-term investments at end of period	$ 215,158	$ 249,555

Amounts shown are unaudited.
See accompanying notes to the financial statements.

THE LUBRIZOL CORPORATION

Notes to Consolidated Financial Statements
Amounts in thousands (except per share data)
September 30, 2003

1. The accompanying unaudited consolidated financial statements contain all adjustments (consisting only of normal recurring accruals unless otherwise noted) necessary to present fairly the financial position as of September 30, 2003 and December 31, 2002, and the results of operations and cash flows for the applicable periods ended September 30, 2003 and 2002.

2. Net income per share is computed by dividing net income by average common shares outstanding during the period, including contingently issuable shares. Net income per diluted share includes the dilutive effect resulting from outstanding stock options and stock awards.

Per share amounts are computed as follows:

	Three Month Period Ended September 30		Nine Month Period Ended September 30	
	2003	2002	2003	2002
Numerator:				
Income before cumulative effect of change in accounting principle	$ 24,298	$ 36,478	$ 79,704	$ 100,782
Cumulative effect of change in accounting principle	-	-	-	(7,785)
Net income	$ 24,298	$ 36,478	$ 79,704	$ 92,997
Denominator:				
Weighted average common shares outstanding	51,717	51,569	51,680	51,475
Dilutive effect of stock				

options and awards	297	172	189	323
Denominator for net income per share, diluted	52,014	51,741	51,869	51,798
Net Income Per Share:				
Income before cumulative effect of change in accounting principle	$ 0.47	$ 0.71	$ 1.54	$ 1.96
Cumulative effect of change in accounting principle	-	-	-	(0.15)
Net income per share	$ 0.47	$ 0.71	$ 1.54	$ 1.81
Diluted Net Income Per Share:				
Income before cumulative effect of change in accounting principle	$ 0.47	$ 0.71	$ 1.54	$ 1.95
Cumulative effect of change in accounting principle	-	-	-	(0.15)
Net income per share, diluted	$ 0.47	$ 0.71	$ 1.54	$ 1.80

Weighted average shares issuable upon the exercise of stock options which were excluded from the diluted earnings per share calculations because they were antidilutive for the three- and nine-month periods ended September 30, 2003 were 2.0 million and 2.7 million, respectively, and for the three- and nine-month periods ended September 30, 2002 were 3.7 million and 1.9 million, respectively.

THE LUBRIZOL CORPORATION

Notes to Consolidated Financial Statements
Amounts in thousands (except per share data)
September 30, 2003

3. Total comprehensive income for the three- and nine-month periods ended September 30, 2003 and 2002 is comprised as follows:

	Three Month Period Ended September 30		Nine Month Period Ended September 30	
	2003	2002	2003	2002
Net income	$ 24,298	$ 36,478	$ 79,704	$ 92,99
Foreign currency translation adjustment	3,618	767	23,168	26,49
Unrealized gains (losses)- natural gas hedges	(267)	-	(757)	
Unrealized gains (losses)- interest rate swaps	434	(836)	1,038	(85
Pension plan minimum liability	158	-	158	

Total comprehensive income	$ 28,241	$ 36,409	$ 103,311	$ 118,63

4. The company aggregates its product lines into four principal operating segments: fluid technologies for transportation, fluid technologies for industry, advanced fluid systems and emulsified products. Fluid technologies for transportation (FTT) is comprised of additives for lubricating engine oils, such as for gasoline, diesel, marine and stationary gas engines and additive components; additives for driveline oils, such as automatic transmission fluids, gear oils and tractor lubricants; and additives for fuel products and refinery and oil field chemicals. In addition, this segment sells additive components and viscosity improvers within its lubricant and fuel additives product lines. The company's fluid technologies for transportation product lines are generally produced in shared manufacturing facilities and sold largely to a common customer base. Fluid technologies for industry (FTI) includes industrial additives, such as additives for hydraulic, grease and metalworking fluids and compressor lubricants; and performance chemicals, such as additives for coatings and inks, defoamers, process chemicals and surfactants for personal care and industrial cleaners. The advanced fluid systems and emulsified products operating segments do not constitute reportable business segments. The results of these two operating segments have been aggregated into the all other segment. Advanced fluid systems is comprised of fluid metering devices, particulate emission trap devices, and FluiPak(TM) sensor systems, and emulsified products is comprised of PuriNOx(TM) low-emissions diesel fuel.

The company primarily evaluates performance and allocates resources based on segment contribution income, defined as revenues less expenses directly identifiable to the product lines aggregated within each segment, as well as projected future returns. In addition, in calculating segment operating profit before tax, the company allocates corporate research, testing, selling and administrative expenses, primarily based upon revenues, and assigns excess capacity costs to the segments to which it applies. The company calculates the cost of excess production capacity at our manufacturing facilities and excludes this amount from product costs when reporting segment gross profit and segment contribution income.

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THE LUBRIZOL CORPORATION

Notes to Consolidated Financial Statements
Amounts in thousands (except per share data)
September 30, 2003

The following table presents a summary of the company's reportable segments for the three- and nine-month periods ended September 30, 2003 and 2002, based on the current reporting structure. Prior-year amounts have been restated to reflect reclassifications of products between reporting segments and changes in allocation methodology of corporate expenses:

	Three Month Period Ended September 30	Nine Month Peri Ended September

	2003	2002	2003	----
Revenues from external customers:				
FTT	$ 382,299	$ 400,736	$ 1,165,891	$ 1
FTI	117,833	102,627	342,008	
All other	9,735	6,940	24,858	
Total revenues	$ 509,867	$ 510,303	$ 1,532,757	$ 1
Segment contribution income(loss):				
FTT	$ 65,440	$ 84,585	$ 222,556	$
FTI	19,005	18,922	55,491	
All other	(1,271)	(2,412)	(5,192)	
Total segment contribution income	$ 83,174	$ 101,095	$ 272,855	$
Segment operating profit(loss) before tax:				
FTT	$ 32,795	$ 45,703	$ 118,551	$
FTI	10,040	13,875	29,791	
All other	(2,696)	(3,471)	(9,729)	
Total segment operating profit before tax	40,139	56,107	138,613	
Restructuring charge	(409)	-	(7,447)	
Interest expense - net	(5,698)	(3,995)	(15,654)	
Income before income taxes and cumulative effect of an accounting change	$ 34,032	$ 52,112	$ 115,512	$

THE LUBRIZOL CORPORATION

Notes to Consolidated Financial Statements
Amounts in thousands (except per share data)
September 30, 2003

5. The company has elected the intrinsic value method to account for employee stock options. The following table shows the pro forma effect on net income and earnings per share if the company had applied the fair value recognition provisions of SFAS 123, "Accounting for Stock-Based Compensation," to stock-based employee compensation:

	Three Month Period Ended September 30		Nine Month Period Ended September 30	
	2003	2002	2003	2002
Reported net income	$ 24,298	$ 36,478	$ 79,704	$ 92,997
Plus: Stock-based employee compensation (net of tax) included in net income	(3)	8	365	114
Less: Stock-based employee				

Amounts in thousands (except per share data)

compensation (net of tax) using the fair value method	(1,078)	(1,517)	(3,881)	(4,551)
Pro forma net income	$ 23,217	$ 34,969	$ 76,188	$ 88,560
Reported net income per share	$ 0.47	$ 0.71	$ 1.54	$ 1.81
Pro forma net income per share	$ 0.45	$ 0.68	$ 1.47	$ 1.72
Reported net income per share, diluted	$ 0.47	$ 0.71	$ 1.54	$ 1.80
Pro forma net income per share, diluted	$ 0.45	$ 0.68	$ 1.47	$ 1.71

6. In February 2003, the company notified employees at its Bromborough, England facility of plans to restructure and reduce operational costs to remain competitive. The facility consolidated various operational activities to achieve greater efficiency through improved business processes. There will be a reduction of 40 employees, or approximately 35% of the facility's headcount, by the end of 2003. These changes began during the first quarter of 2003 and are expected to be completed by the end of 2003. As a result of these changes, the company recorded a restructuring charge for Bromborough of $.4 million in the third quarter and $6.7 million in the first nine months of 2003. The charge in the third quarter was primarily due to severance costs. The charge in the first nine months of 2003 consisted of $3.2 million in severance costs, $3.3 million in asset impairments and $.2 million in other miscellaneous costs. Cash expenditures in the third quarter of 2003 were $.4 million and in the first nine months of 2003 were $2.9 million. An accrued liability of $.5 million remains at September 30, 2003, relating to employee severance costs. Additional severance costs of approximately $.3 million are expected to be incurred during the remainder of 2003 for those employees that will be separated after 90 days of the legal notification date of the restructuring. The restructuring charge in the first nine months of 2003 also includes $.7 million for a voluntary separation program to employees at the company's India joint venture, Lubrizol India Private Limited, which is accounted for using the consolidated method. Cash expenditures for India were $.7 million in both the second quarter and the first nine months of 2003. The charge for both cost reduction initiatives are reported as a

separate line item in the consolidated income statement, entitled "Restructuring charge" and are included in the "Total cost and expenses" subtotal on the consolidated income statement. The charge relates primarily to the fluid technologies for transportation segment. The following table shows the reconciliation of the September 30, 2003 liability balance for the third quarter of 2003 and the first nine months of 2003:

	Three Month Period Ended September 30, 2003	Nine Month Period Ended September 30, 2003
Beginning balance	$ 500	$ -
Restructuring charge	409	7,447
Less cash paid	(356)	(3,581)
Less asset impairments		(3,327)
Translation adjustments	1	15
September 30, 2003 Balance	$ 554	$ 554

On November 4, 2003 the company announced workforce reductions, primarily in the United States, designed to improve profitability to reposition the company for stronger growth. The reductions are expected to be completed by year-end, 2003 and are estimated to result in annual pretax savings of approximately $15 million beginning in 2004. These savings are in addition to approximately $4.5 million of pre-tax savings from the restructuring programs at Bromborough and India. The company will record a fourth quarter, 2003 restructuring charge that is projected to be approximately $13 million.

7. The company has various financial instruments, including cash and short-term investments, investments in nonconsolidated companies, foreign currency forward contracts, commodity hedges, interest rate swaps and short- and long-term debt. The company has determined the estimated fair value of these financial instruments by using available market information and generally accepted valuation methodologies. The use of different market assumptions or estimation methodologies could have a material effect on the estimated fair value amounts. The company uses derivative financial instruments including interest rate and commodity hedges and forward foreign currency exchange contracts to manage market risks. The company does not use derivative financial instruments for trading purposes.

The company recognizes all derivatives on the balance sheet at fair value and establishes criteria for designation and effectiveness of hedging relationships. Derivatives that are not hedges must be adjusted to fair value through income. Depending upon the nature of the hedge, changes in fair value of the derivative are either offset against the change in fair value of assets, liabilities or firm commitments through earnings or recognized in other comprehensive income until the hedged item is recognized in earnings. The ineffective portion of a derivative's change in value is immediately recognized in earnings.

The company is exposed to the effect of changes in commodity prices for natural gas and electric utility expenses on its earnings and cash flow. In the second quarter of 2003, the company modified its commodity hedging program for natural gas and electricity purchasing by using financial instruments to reduce the volatility on earnings of utility expense. These contracts relate to transactions with maturities of less than one year and

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Notes to Consolidated Financial Statements
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September 30, 2003

are accounted for as cash flow hedges and any effective unrealized gains or losses on open contracts are recorded in other comprehensive income, net of tax. At September 30, 2003 open contracts totaled $7.0 million. A hedge liability was recorded at September 30, 2003 of $1.2 million, which represents the unrealized loss at that date based upon current futures prices. The loss, net of deferred taxes of $.4 million, is included as a charge of $.8 million in other comprehensive income loss. The company expects all of the unrealized hedge gains or losses to be reclassified into earnings within the next 12 months.

8. In the third quarter of 2003, the company completed two acquisitions in the fluid technologies for industry segment for cash of $67.5 million. In July, 2003 the company purchased the product lines of the North American-based silicones business from BASF, which expanded our foam control additives business to about $40 million in annual revenues. Assets acquired from BASF included customer lists, certain trademarks, manufacturing technology and other related intellectual property specifically developed for silicone products in the North America region, and finished goods inventory. Silicones are used in the manufacture of sealants, caulks and water proofing products. Historical annual revenues for these silicone products approximate $6 million. In late September, 2003 the company completed an acquisition of selected personal care ingredients business from Amerchol Corporation, a subsidiary of The Dow Chemical Company. Products from this business go into a wide range of end uses, including skin care and hair conditioners. Products include methyl glucoside derivatives, lanoline derivatives and Promulgen(TM) personal care ingredients. Annualized revenues of the acquisition are approximately $30 million.

The company is currently in the process of allocating the purchase price for both of these acquisitions, so it is possible the assignment of value among assets acquired may change once the purchase price allocation is complete.

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THE LUBRIZOL CORPORATION

Item 2 - Management's Discussion and Analysis of
Financial Condition and Results of Operations

RESULTS OF OPERATIONS

Our revenues in the third quarter of 2003 were generally even with revenues in the same period in 2002 and increased in the first nine months of 2003 compared with the first nine months of 2002. However, net income decreased in both the third quarter and first nine months of 2003 compared to the same periods in 2002. The primary operating drivers of the lower earnings were lower shipment volume, higher average raw material cost and higher manufacturing expenses, which more than offset a higher average selling price. A detailed discussion of these and other factors that affected the third quarter and nine months follows.

We group our product lines into three reportable segments: fluid technologies for transportation, fluid technologies for industry and all other. Fluid technologies for transportation comprised approximately 76% of our consolidated revenues and 86% of our segment pre-tax operating profits in the first nine months of 2003. See Note 4 to the financial statements for further financial disclosures by reporting segment.

Our consolidated revenues decreased $.4 million, or less than 1%, in the third quarter of 2003 compared with the same period in 2002, due to a 10% decline in shipment volume that was partially offset by a 9% increase in average selling price. Excluding the impact of acquisitions (Dock Resins Corporation, Intermountain Specialties, Inc., also known as Brose Chemical Company, and certain product lines of BASF), third quarter revenues decreased $6.6 million, or 1%, compared with the third quarter of the prior year. Consolidated revenues increased $46.6 million, or 3%, in the first nine months of 2003 compared with the same period in 2002, due to an 8% increase in average selling price, partially offset by a 5% decline in shipment volume. Excluding the impact of acquisitions (Kabo Unlimited, Inc., Dock, Chemron, Brose and certain product lines of BASF), revenues increased $13.7 million, or 1%, in the first nine months of 2003 compared with 2002, due to an 8% increase in average selling price and higher revenues by our equipment companies, partially offset by an 8% decline in shipment volume.

The following table shows our shipment volume by geographic zone in the third quarter and the first nine months of 2003.

	3rd Qtr 2003 Volume	YTD 2003 Volume
North America	46%	46%
Europe	28%	28%
Asia-Pacific/Middle East	19%	19%
Latin America	7%	7%
Total	100%	100%

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THE LUBRIZOL CORPORATION

Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operations

Changes in our shipment volume vary in different geographic zones. The following table shows the changes in shipment volume by geographic zone in the third quarter and first nine months of 2003 compared with the same periods in 2002.

	3rd Qtr 2003 vs. 2002 Increase (Decrease)		YTD 2003 vs. 2002 Increase (Decrease)	
	Total	Excluding Acquisitions	Total	Excluding Acquisitions

North America	(13%)	(14%)	(5%)	(10%)
Europe	(13%)	(13%)	(9%)	(9%)
Asia-Pacific/Middle East	(3%)	(3%)	(5%)	(5%)
Latin America	8%	8%	4%	4%
Total	(10%)	(11%)	(5%)	(8%)

Excluding acquisitions, total shipment volume decreased 11% in the third quarter of 2003 and 8% in the first nine months of 2003 compared with the same periods in 2002. Approximately 9% of the decrease in the third quarter of 2003 and 25% of the decrease in the first nine months of 2003 was due to a shift in our viscosity modifier product line from liquids to a higher-value concentrated solid form. All zones were affected by the shift to solid viscosity modifiers, though the effects were mostly seen in North America and Europe. The remaining shipment volume decrease for both periods was primarily due to losses associated with a major international customer, which mainly affected North America and Europe, along with weak worldwide demand for lubricants. We believe that the severe acute respiratory syndrome (SARS) outbreak in Southeast Asia along with weakness stemming from economic and political conditions within certain countries of the Asia-Pacific / Middle East region contributed to the decline in the Asia-Pacific / Middle East zone during the first nine months of 2003. See the "Segment Analysis" section for additional explanation of shipment volume variances by business segment and geographic zone in 2003 compared with 2002.

Our average additive selling price increased 9% in the third quarter of 2003 compared to the same period in 2002 due to a 6% increase in the combination of price and product mix and 3% favorable currency effects. Our average additive selling price increased 8% in the first nine months of 2003 compared to the first nine months of 2002 equally due to favorable currency effects and an increase in the combination of price and product mix. Sequentially, the third quarter 2003 average additive selling price was even with the second quarter and 3.5% higher than the first quarter of 2003, due to favorable currency effects and the implementation of a price increase in the form of a surcharge at the end of the first quarter of 2003. This surcharge was designed to cover the continuing rise in raw material prices and natural gas-fired utility costs, since our last price increase in the fourth quarter of 2002.

Our cost of sales increased $18.6 million, or 5% ($14.4 million, or 4%, excluding acquisitions), in the third quarter of 2003 and $66.5 million, or 6% ($43.2 million, or 4%, excluding acquisitions), in the first nine months of 2003 compared with the same periods in 2002. The increase for both periods was primarily due to higher average raw material cost and higher manufacturing expenses. Average raw material cost increased 11% in the third quarter of 2003 and 9% in the first nine months of 2003 compared with the same periods of 2002 primarily due to higher raw material prices, mainly driven by higher prices of crude oil and natural gas, and unfavorable currency effects. Sequentially, average raw material cost in the third quarter of 2003 increased 2% from the second quarter of 2003.

Total manufacturing expenses increased 15% (14% excluding acquisitions) in the third quarter of 2003 and 13% (11% excluding acquisitions) in the first nine months of 2003 compared with the same periods in 2002. We built inventories in the third quarter of 2002 and drew down inventories in the third quarter of 2003. Excluding acquisitions and the impact of changes in inventory levels, manufacturing expenses increased 7% in the third quarter of 2003 and 10% in the first nine months of 2003 compared with the same periods in 2002, primarily due to unfavorable currency effects, higher utilities and higher salary and benefit expenses, partially offset by a reduction in variable pay expense. In addition, total manufacturing expenses included a reclassification of expenses at certain subsidiaries of our fluid technologies for industry (FTI) and advanced fluid systems (AFS) operating segments that were charged in 2002 to selling and administrative expenses or material costs. The reclassification increased manufacturing expenses by $.9 million in the third quarter of 2003 and $3.6 million in the first nine months of 2003. We estimate the total impact of this reclassification to manufacturing expenses for 2003 will be approximately $5.0 million.

Cost of sales for the first nine months of 2003 included approximately $3 million in manufacturing expenses to cover costs associated with two fires that occurred during the second quarter of 2003. In April 2003, an after-working-hours fire destroyed a metalworking additive blending facility we leased in Detroit. There were no injuries, nor any damage to a nearby warehouse where we stored finished goods. We were able to supply customers from this warehouse and we have permanently shifted production to our Painesville, Ohio plant. Also in April 2003, a fire associated with a maintenance shutdown occurred in a dispersant production unit at our plant in Le Havre, France.

Gross profit (net sales less cost of sales) decreased $19.0 million, or 13% ($21.0 million, or 14%, excluding acquisitions), in the third quarter of 2003 and $19.8 million, or 5% ($29.3 million, or 7%, excluding acquisitions), in the first nine months of 2003 compared with the same periods in 2002. The decrease for both periods was primarily due to lower shipment volume, higher average raw material cost and higher manufacturing expenses, partially offset by higher average selling price. Our gross profit percentage (gross profit divided by net sales) decreased to 25.9% for the third quarter of 2003 and 26.9% for the first nine months of 2003, compared with 29.6% in the third quarter of 2002 and 29.1% in the first nine months of 2002. The decrease in the gross profit percentages for both periods was due to the reasons previously described. The impact of acquisitions and the reclassification of certain expenses to manufacturing, as described above, accounted for a decrease of 60 basis points (of the total 220 basis point decline) in our gross profit percentage in the first nine months of 2003. Sequentially, the gross profit percentage decreased from 27.5% in the second quarter of 2003.

Our selling and administrative expenses decreased $.9 million, or 2% ($1.5 million, or 3%, excluding acquisitions), in the third quarter of 2003 and increased $2.9 million, or 2% (decreased $.1 million excluding acquisitions), in the first nine months of 2003 compared with the same periods in 2002. Excluding acquisitions, the decrease for both periods was primarily due to a reduction in our variable pay expense and the reclassification of certain 2002 selling and administrative expenses for our FTI and AFS operating segments, which was partially offset by unfavorable currency effects and higher salary and benefit expenses.

Our research, testing and development expenses (technology expenses) decreased $1.8 million, or 4% ($2.1 million, or 5%, excluding acquisitions), in the third quarter of 2003 and $1.4 million, or 1% ($2.7 million, or 2%, excluding acquisitions), in the first nine months of 2003 compared with the same periods in 2002. The decrease for both periods, excluding acquisitions, was due to lower testing at outside laboratories and a reduction in our variable pay expense, partially offset by unfavorable currency effects. In addition, technology expenses included a write-down of $1.1 million in the first nine months of 2003 related to a former technical facility in Japan that we sold during the third quarter of 2003.

In the first nine months of 2003, we recorded a restructuring charge of $7.4 million, or $.10 per share, consisting of $6.7 million for our Bromborough, England intermediate production and blending facility and $.7 million for a voluntary separation program at our joint venture in India. The Bromborough charge primarily consisted of $3.2 million in employee separation benefits and $3.3 million in asset impairments for production units taken out of service. In the third quarter the Bromborough charge was $.4 million, or $.01 per share, for severance costs. We have eliminated some capacity at this facility and have planned a reduction of 40 positions. We expect the Bromborough restructuring initiative will be completed by year-end. We estimate the full year restructuring charge will be approximately $7.5 million, or $.10 per share, and total annualized savings from the combined restructuring activities are projected to be $4.5 million, of which approximately $2.0 million is expected to be realized in 2003.

The change in other income (expense) favorably affected pre-tax income by $.5 million in the third quarter of 2003 and $4.2 million in the first nine months of 2003 compared with the same periods in 2002. The favorable variance for the first nine months of 2003 was primarily due to increased currency translation gains.

Interest income decreased $.9 million in the third quarter of 2003 and $2.0 million in the first nine months of 2003 compared with the same periods in 2002 as a result of lower interest rates. Interest expense increased $.8 million in the third quarter of 2003 and $1.7 million in the first nine months of 2003, compared with the same periods in 2002, due to the absence of the interest rate swap agreements that we utilized in the third quarter of 2002 and, in the third quarter of 2003, interest on a European tax settlement. In 2002, we had swap agreements that reduced interest expense by approximately $.8 million ($.3 million impact from outstanding swap and $.5 million amortization of deferred gain) in the third quarter of 2002 and $3.6 million ($3.1 million impact from outstanding swap and $.5 million amortization of deferred gain) in the first nine months of 2002. As a result of the interest rate swap agreements that were terminated in 2002, the unrecognized gain is being amortized as a reduction of interest expense through December 1, 2008. Amortization of the unrealized gain reduced interest expense in the third quarter of 2003 by approximately $.7 million and in the first nine months of 2003 by approximately $2.0 million.

As a result of the above factors, our income before income taxes and the cumulative effect of a change in accounting principle decreased 35% to $34.0 million in the third quarter of 2003, and 20% to $115.5 million in the first nine months of 2003, compared with $52.1 million and $144.0 million for the respective corresponding periods in 2002.

We had an effective tax rate of 28.6% for the third quarter of 2003 and 31.0% for the first nine months of 2003, compared with 30.0% for both periods in 2002. The lower effective tax rate in the third quarter of 2003 increased earnings by $.01 per share and the higher effective tax rate for the first nine months of 2003 reduced earnings by $.03 per share, compared to the same periods in 2002. The increase in the effective tax rate for the first nine months of 2003, as compared to the first nine months of 2002, mainly was due to a non-recurring 2002 charitable contribution of technology, offset in part by the impact of higher expected levels of non-taxable currency translation gains.

We lowered our estimated 2003 effective tax rate in both the second quarter and the third quarter, mainly due to higher expected levels of non-taxable currency translation gains for the full year.

As a result of the factors described above, income before the cumulative effect of a change in accounting principle decreased $12.2 million, or 33% in the third quarter of 2003 and $21.1 million, or 21%, in the first nine months of 2003 compared with the same periods in 2002. Income per share, before the cumulative effect of a change in accounting principle, was $.47 in the third quarter of 2003 and $1.54 in the first nine months of 2003, compared with $.71 and $1.96 for the respective corresponding periods in 2002.

During the first half of 2002, we completed the impairment analysis required for Statement of Financial Accounting Standards 142 (SFAS 142), "Goodwill and Other Intangible Assets," which we adopted on January 1, 2002. There was no impairment either in the fluid technologies for transportation segment or in the fluid technologies for industry operating segment. However, for the advanced fluid systems operating segment, which is included in the all other reporting segment, we recorded an impairment of $7.8 million, thus eliminating all the goodwill for the all other reporting segment. The charge was recorded as a cumulative effect of a change in accounting principle as of January 1, 2002.

Primarily as a result of the above factors, our net income in the third quarter of 2003 decreased 33% to $24.3 million ($.47 per share), compared with $36.5 million ($.71 per share) in the third quarter of 2002. Net income in the first nine months of 2003 decreased 14% to $79.7 million ($1.54 per share) compared with $93.0 million ($1.81 per share) in the first nine months of 2002.

On November 4, 2003 the company announced workforce reductions, primarily in the United States, designed to improve profitability to reposition the company for stronger growth. The reductions are expected to be completed by year-end, 2003 and are estimated to result in annual pretax savings of approximately $15 million beginning in 2004. These savings are in addition to approximately $4.5 million of pre-tax savings from the restructuring programs at Bromborough and India. The company will record a fourth quarter, 2003 restructuring charge that is projected to be approximately $13 million.

SEGMENT ANALYSIS

A description of the company's operating segments along with the products, services and markets for each of the operating segments is included in Note 4 to the financial statements. Prior year amounts have been restated to reflect reclassifications of products among the reportable segments.

OPERATING RESULTS BY BUSINESS SEGMENT

(in Millions of Dollars)	Three Month Period Ended September 30 2003	2002	Nine Month Period Ended September 30 2003	200
Revenues:				
Fluid technologies for transportation	$ 382.3	$ 400.7	$ 1,165.9	$ 1,
Fluid technologies for industry	117.8	102.6	342.0	
All other	9.8	7.0	24.9	
Total	$ 509.9	$ 510.3	$ 1,532.8	$ 1,
Gross Profit:				
Fluid technologies for transportation	$ 104.7	$ 123.9	$ 335.6	$
Fluid technologies for industry	35.9	33.8	104.2	
All other	2.6	1.9	6.4	
Total	$ 143.2	$ 159.6	$ 446.2	$
Segment Contribution Income(Loss):				
Fluid technologies for transportation	$ 65.4	$ 84.6	$ 222.6	$
Fluid technologies for industry	19.0	18.9	55.5	
All other	(1.3)	(2.4)	(5.2)	
Total	$ 83.1	$ 101.1	$ 272.9	$

Fluid Technologies for Transportation Segment

Segment revenues decreased $18.4 million, or 5%, in the third quarter of 2003 compared with the same period in 2002, due to a 13% decline in shipment volume, partially offset by an 8% increase in average selling price. The increase in average selling price for the third quarter of 2003 primarily was due to an increase in the combination of price and product mix along with 3% favorable currency effects. Segment revenues decreased $21.4 million, or 2%, in the first nine months of 2003 compared with the first nine months of 2002 due to a 10% decrease in shipment volume partially offset by an 8% increase in average selling price. The increase in average selling price in the first nine months of 2003 primarily was due to favorable currency effects of 5% and the remainder was due to an increase in the combination of price and product mix.

The fluid technologies for transportation segment implemented a price increase in December 2002 for the North America zone and in January 2003 for the rest of the world. In addition, a second price increase that was structured as a surcharge was implemented in late March for North America and in late April for products sourced from Asia and Latin America as well as select products in Europe. This surcharge was designed to cover the continuing rise in raw material prices and natural gas-fired utility costs, since our last price increase in the fourth quarter of 2002.

The following table shows the changes in shipment volume by geographic zone in the third quarter and first nine months of 2003 compared with the same periods in 2002.

	3rd Qtr 2003 vs. 2002 Increase (Decrease)	YTD 2003 vs. 2002 Increase (Decrease)
North America	(18%)	(13%)
Europe	(15%)	(9%)
Asia-Pacific/Middle East	(4%)	(6%)
Latin America	7%	3%
Total	(13%)	(10%)

The shipment volume decline in both the third quarter and the first nine months of 2003 partially was due to lower unit sales of viscosity modifiers, principally caused by a shift from liquid polymers to solid polymers. Generally, solids are one-tenth the volume of liquids. Excluding this shift in our viscosity modifier product line, total shipment volume decreased 12% in the third quarter and 8% in the first nine months of 2003. About half of the shipment volume decreases in North America and Europe were due to losses in our engine oils business and specialty driveline business associated with a major international customer. The declines in North America for the third quarter and the first nine months of 2003 also were due to our shifting of some products in our specialties business to more concentrated formulations. In addition, weak worldwide demand for lubricants contributed to the declines in the North America and Europe zones for both the third quarter and the first nine months of 2003. The third quarter decrease in Asia-Pacific/Middle East volume primarily was due to the weak business environment stemming from economic and political conditions in certain parts of this region. During the first nine months of 2003, we believe SARS also negatively impacted business activity primarily in the Asia-Pacific / Middle East zone.

Segment gross profit decreased $19.2 million, or 16%, in the third quarter of 2003 and $23.0 million, or 6%, in the first nine months of 2003 compared with the same periods in 2002. The decrease for both periods primarily was due to lower shipment volume, higher average raw material cost and higher manufacturing expenses, partially offset by higher average selling price due to favorable currency effects and an increase in the combination of price and product mix. In calculating gross profit at the operating segment level, we exclude our estimate of the cost of excess capacity from product costs (See Note 4 to the financial statements.) The gross profit percentage for this segment was 27.4% in the third quarter of 2003 and 28.8% in the first nine months of 2003, compared with 30.9% and 30.2% in the respective comparable periods in 2002. The decrease in the gross profit percentage for both comparison periods was due to the reasons previously explained.

Direct selling, marketing and technical expenses were flat in the third quarter of 2003 and decreased $3.3 million, or 3%, in the first nine months of 2003 compared with the same periods in 2002, primarily due to lower technical spending at outside test laboratories. Segment contribution income decreased $19.1 million, or 23%, in the third quarter of 2003 compared with the third quarter of 2002 entirely due to lower gross profit. Segment contribution income decreased $20.8 million, or 9%, in the first nine months of 2003 compared with the same period in 2002 as a result of lower gross profit and lower equity earnings, partially offset by lower technical expenses.

THE LUBRIZOL CORPORATION

Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operations

Fluid Technologies for Industry Segment

Segment revenues increased $15.2 million, or 15% ($8.9 million, or 9%, excluding acquisitions), in the third quarter of 2003 and $62.1 million, or 22% ($29.2 million, or 10%, excluding acquisitions), in the first nine months of 2003 compared with the same periods in 2002. Acquisitions contributed $6.2 million of the segment revenue increase in the third quarter of 2003, due to Dock Resins, Brose and the product lines of BASF, and $32.9 million of the segment revenue increase in the first nine months of 2003, primarily due to Dock Resins and Chemron. The 9% increase in segment revenues during the third quarter of 2003, excluding acquisitions, was due to a 5% increase in shipment volume along with a 4% increase in average selling price compared to the third quarter of 2002. The 10% increase in segment revenues during the first nine months of 2003, excluding acquisitions, was primarily due to a 9% increase in shipment volume.

The shipment volume increase in both periods primarily was due to ongoing business growth as the result of new business gains and the introduction of new products in our personal care, defoamers, specialty monomers and mining chemicals businesses. The third quarter increase in average selling price primarily was due to 3% favorable currency effects and a slight increase in the combination of price and product mix, partially due to favorable product mix in our personal care business. Average selling price increased 1% for the first nine months of 2003 compared with the same period in 2002, due to 4% favorable currency effects partially offset by a decrease in the combination of price and product mix. The decrease occurred in our inks additives business, specialty monomers business and compressor lubricant business and primarily was due to lower priced product mix. Slightly higher royalty income in our synthetic refrigerant lubricants business of $.1 million in the third quarter of 2003 and $.5 in the first nine months of 2003, compared with the same periods in 2002, also contributed to the increased segment revenues.

The following table shows the changes in shipment volume by geographic zone in the third quarter and first nine months of 2003 compared with the same periods in 2002.

	3rd Qtr 2003 vs. 2002 Increase (Decrease)		YTD 2003 vs. 2002 Increase (Decrease)	
	Total	Excluding Acquisitions	Total	Excluding Acquisitions
North America	8%	2%	32%	7%
Europe	7%	7%	10%	10%
Asia-Pacific / Middle East	15%	15%	18%	18%
Latin America	27%	27%	15%	15%
Total	9%	5%	25%	9%

Excluding acquisitions, the increase in the third quarter of 2003 for North America and Europe primarily was due to increases in the coatings and inks business. The shipment volume increase in North America in the first nine months of 2003 primarily was due to the 2002 acquisitions of Chemron and Dock Resins. Excluding acquisitions, the increase in North America in the first nine months of 2003 partially was due to market share gains in our personal care and compressor lubricant businesses along with increases in the coatings and inks business from the introduction of new products. The increase in Europe in the first nine months of 2003 was related to increases in our metalworking and compressor lubricant businesses and new applications in our specialty monomers business. The increase in the third quarter of 2003 for the Asia-Pacific / Middle East zone was spread across many of the FTI businesses. Approximately

half of the increase in the first nine months of 2003 for Asia-Pacific / Middle East was due to increased shipments in our metalworking business as a result of a distributor relationship that was terminated at the beginning of 2002. Our metalworking sales in this zone in the first half of 2002 were below normal levels because our customers were buying from the distributor's inventory. Our customers subsequently resumed purchasing the products from us, beginning in the second half of 2002. The increase in Latin America in both the third quarter of 2003 and the first nine months of 2003 was due to a shift of our specialty emulsifiers business with some of our existing customers from North America to Latin America along with some business gains in our coatings and inks business.

Segment gross profit increased $2.1 million, or 6% ($.1 million, or less than 1%, excluding acquisitions), in the third quarter of 2003, and $8.6 million, or 9% ($.9 million decrease, or 1%, excluding acquisitions), in the first nine months of 2003 compared with the same periods in 2002. Excluding acquisitions, the third quarter increase was due to higher shipment volume that was partially offset by higher manufacturing expenses. The increase in manufacturing expenses primarily was due to the reclassification to manufacturing expenses of $.9 million in FTI expenses charged in 2002 as selling and administrative expenses, and costs associated with the integration of a multi-purpose chemical production facility in Spartanburg, South Carolina that was purchased in the second quarter of 2003. In addition, unfavorable product mix in the anti-wear hydraulics business lowered segment gross profit in the third quarter of 2003. Excluding acquisitions, the decrease in segment gross profit in the first nine months of 2003 was due to higher manufacturing expenses and higher average raw material cost, which more than offset higher shipment volume and higher average selling price. The increase in manufacturing expenses primarily was due to the reclassification to manufacturing expenses of $3.6 million of FTI expenses charged in 2002 as selling and administrative expenses, and costs relating to the fire at the Detroit manufacturing facility. The gross profit percentage for this segment was 30.6% in the third quarter of 2003 and 33.1% in the first nine months of 2003, compared with 30.6% and 34.3% in the respective corresponding periods in 2002. The decrease in the gross profit percentage for the first nine months of 2003 compared with the same period in 2002 was due to the impact of the Chemron acquisition, higher raw material costs and increased manufacturing expenses as a result of the metalworking fire and the reclassification of certain FTI selling and administrative expenses to manufacturing expenses.

Segment contribution income increased $.1 million, or less than 1%, in the third quarter of 2003 and increased $1.9 million, or 4%, in the first nine months of 2003 compared with the same periods in 2002. The increase for both periods primarily was due to higher gross profit, partially offset by higher direct technical and selling expenses and higher amortization expenses resulting from

2002 acquisitions.

WORKING CAPITAL, LIQUIDITY AND CAPITAL RESOURCES

Cash provided by operating activities was $113.7 million in the first nine months of 2003 compared with $173.2 million in the first nine months of 2002. The decrease in cash from operating activities of $59.5 million in the first nine months of 2003 primarily was due to lower earnings and an increase in working capital items. Increased receivables consumed cash of $18.8 million, partially due to fire insurance receivables in 2003 of approximately $5.0 million to reimburse the company for expenditures associated with the fire. In addition, average days sales outstanding in the first nine months of 2003 were 54.5 days, compared with 53.5 days in the first nine months of 2002. Increased inventory consumed cash of $13.3 million, due to higher unit values, some slowing of sales and a build-up of strategic stock in certain key materials to ensure customers of supply and to protect them during planned maintenance shutdowns. We paid down accounts payable and accrued liabilities by $24.3

million since year-end compared with a build up of $4.7 million in the first nine six months of 2002, due to the timing of procurement and payment to vendors. We have not changed our payment terms to suppliers.

Our capital expenditures in the first nine months of 2003 were $59.5 million, compared with $46.0 million for same period in 2002. In 2003, we estimate capital expenditures will be in the range of $80 million to $90 million as compared with $65.3 million in 2002. Capital expenditures included the purchase of a multipurpose chemical production facility in Spartanburg, South Carolina with additional adjacent land in April 2003 for $2.8 million. The facility is capable of producing several products used in a variety of applications for the fluid technologies for industry segment.

We completed two acquisitions in the third quarter of 2003 for $67.5 million. In July, 2003 we purchased the product lines of the North American-based silicones business from BASF, which expands our foam control additives business to about $40 million in annual revenues. Assets acquired from BASF's North American-based silicones business included customer lists, certain trademarks, manufacturing technology and other related intellectual property specifically developed for silicone products in the North America region, and finished goods inventory. Silicones are used in the manufacture of sealants, caulks and water proofing products. Historical annual revenues for these silicone products approximate $6 million. In late September, 2003 we completed an acquisition of selected personal care ingredients business from Amerchol Corporation, a subsidiary of The Dow Chemical Company. Products from this business go into a wide range of end uses, including skin care and hair conditioners. Products include methyl glucoside derivatives, lanoline derivatives and Promulgen(TM) personal care ingredients. Historical annualized revenues of this acquisition approximate $30 million.

Our net debt to capitalization ratio at September 30, 2003 was 18.0%. Net debt is the total of short- and long-term debt, reduced by cash and short-term investments in excess of an assumed operating cash level of $40 million and excluding unrealized gains and losses on derivative instruments designated as fair value hedges of fixed rate debt. Capitalization is shareholders' equity plus net debt. Total debt as a percent of capitalization was 28.9% at September

30, 2003.

Our share repurchase program has been suspended indefinitely as we are holding our financial resources in reserve for future acquisitions. Primarily as a result of all of the above activities and the payment of dividends, our balance of cash and short-term investments decreased $51.3 million at September 30, 2003 compared with December 31, 2002.

We made a U.S. pension contribution for the 2002 plan year of approximately $3.6 million late in September 2003. We also anticipate making a 2003 plan year contribution of approximately $3.0 million in September 2004. This latter amount may change depending on asset and liability valuations as of year end.

Our financial position remains strong with a ratio of current assets to current liabilities of 3.1 to 1 at September 30, 2003, compared with 3.0 to 1 at December 31, 2002. We currently have $350 million of committed revolving credit facilities that will expire in July 2006. We had an additional $175 million of committed revolving credit facilities that expired in July 2003, which we chose not to renew. We believe our existing credit facilities, internally generated funds and ability to obtain additional financing, if desired, will be sufficient to meet our future capital needs, including acquisitions to expand into new and existing fluid technology markets.

In the second quarter of 2003, we modified our commodity hedging program for natural gas and electricity purchases by using financial instruments. These contracts are accounted for as cash flow hedges and any effective unrealized gains or losses on open contracts are recorded in other comprehensive income, net of tax. At September 30, 2003, open contracts totaled $7.0 million. Maturities ranged from one to twelve months. A hedge liability was recorded at September 30, 2003 of $1.2 million, which represented the unrealized loss at that date based upon current future prices as of that date. The loss, net of deferred taxes of $.4 million, was included as a charge of $.8 million in other comprehensive income loss.

CAUTIONARY STATEMENT FOR SAFE HARBOR PURPOSES

This Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements within the meaning of the federal securities laws. As a general matter, forward-looking statements are those focused upon future plans, objectives or performance as opposed to historical items and include statements of anticipated events or trends and expectations and beliefs relating to matters not historical in nature. Such forward-looking statements are subject to uncertainties and factors relating to our operations and business environment, all of which are difficult to predict and many of which are beyond our control. These uncertainties and factors could cause our actual results to differ materially from those matters expressed in or implied by such forward-looking statements.

We believe that the following factors, among others, could affect our future performance and cause our actual results to differ materially from those expressed or implied by forward-looking statements made in this quarterly report:

- the overall demand for lubricant and fuel additives on a worldwide basis, which has a slow growth rate in mature markets such as North America and Europe;

- the effect on our business resulting from economic and political uncertainty within the Asia-Pacific, Middle East and Latin American regions;

- the lubricant additive demand in developing regions such as China and India, which geographic zones are an announced focus of our activities;

- the potential negative impact on product pricing and shipment volume demand from the consolidation of finished lubricant marketers;

- the degree of competition resulting from lubricant additive industry overcapacity;

- technology developments that affect longer-term trends for lubricant additives, such as improved equipment design, fuel economy, longer oil drain intervals, alternative fuel powered engines and emission system compatibility;

- the overall global economic environment, which affects the operating results of fluid technologies for industry in particular;

- the extent to which we are successful in expanding our business in new and existing fluid technology markets incorporating chemicals, systems and services for industry and transportation;

- our ability to identify, complete and integrate acquisitions for profitable growth;

- our success at continuing to develop proprietary technology to meet or exceed new industry performance standards and individual customer and original equipment manufacturers' expectations;

- the frequency of change in industry performance standards, which affects the level and timing of our technology costs, the product life cycles and the relative quantity of additives required for new specifications;

- our ability to continue to reduce complexities and conversion costs and modify our cost structure to maintain and enhance our competitiveness;

- our success in strengthening relationships and growing business with our largest customers, including those with affiliated lubricant additive companies, and retaining the business of our largest customers over extended time periods;

- the cost, availability and quality of raw materials, including petroleum-based products;

- the cost and availability of energy, including natural gas and electricity;

- the effects of fluctuations in currency exchange rates upon our reported results from international operations, together with non-currency risks of investing in and conducting significant operations in foreign countries, including those relating to political, social, economic and regulatory factors;

- the extent to which we achieve market acceptance of our PuriNOx(TM) low-emission, water-blend fuel product;

- significant changes in government regulations affecting environmental compliance.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We operate manufacturing and blending facilities, laboratories and offices around the world and utilize fixed and variable rate debt to finance our global operations. As a result, we are subject to business risks inherent in non-U.S. activities, including political and economic uncertainties, import and export limitations, and market risks related to changes in interest rates, commodity prices and foreign currency exchange rates. We believe the political and economic risks related to our foreign operations are largely mitigated due to the stability of the countries in which our largest foreign operations are located.

In the normal course of business, we use derivative financial instruments including interest rate and commodity hedges and forward foreign currency exchange contracts to manage our market risks. Our objective in managing our exposure to changes in interest rates is to limit the impact of such changes on earnings and cash flow and to lower our overall borrowing costs. Our objective in managing our exposure to changes in foreign currency exchange rates is to reduce volatility of our earnings and cash flow associated with such changes. Our principal currency exposures are the euro, the pound sterling, the Japanese yen and certain Latin American currencies. Our objective in managing our exposure to changes in commodity prices is to reduce the volatility on earnings of utility expense. We do not purchase derivatives for trading purposes.

Our primary commodity hedge exposures relate to natural gas and electric utility expenses. The calculation of potential loss in fair value is based on an immediate change in the U.S. dollar equivalent balances of our commodity exposures due to a 10% shift in the underlying commodity prices. The potential loss in cash flow and income before tax is based on the change in cash flow and income before tax over a one-year period resulting from an immediate 10% change in commodity prices. A hypothetical 10% increase in commodity prices for the first nine months of 2003 would have had a favorable impact and a hypothetical 10% decrease in commodity prices would have had an unfavorable impact on fair value of $.6 million, cash flow of $.6 million, and income before tax of $.6 million in 2003.

A quantitative and qualitative discussion about our market risk is contained on page 21 of our 2002 Annual Report to our shareholders. There have been no material changes in the market risks faced by us since December 31, 2002.

Item 4. Controls and Procedures

We carried out an evaluation, under the supervision and with the participation of our chief executive officer and chief financial officer, of the effectiveness of our disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e)) as of September 30, 2003. Based on that evaluation, our chief executive officer and chief financial officer concluded that, as of September 30, 2003, our disclosure controls and procedures are effective in timely alerting them to material information relating to the company and its consolidated subsidiaries required to be included in our periodic SEC filings. There were no significant changes in our internal control over financial reporting that occurred during the third quarter of 2003 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

THE LUBRIZOL CORPORATION

PART II. OTHER INFORMATION

Item 2. Changes in Securities and Use of Proceeds

(c) On September 4, 2003, we issued 1,500 common shares in a private placement transaction exempt from registration under the Securities Act of 1933 pursuant to Section 4(2) of that Act. We issued the shares to a consultant as partial payment for services rendered in accordance with a consulting agreement.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

31 Rule 13a-14(a) Certifications

32 Certification of Chief Executive Officer and Chief Financial Officer of The Lubrizol Corporation Pursuant to 18 U.S.C. Section 1350

(b) Reports on Form 8-K

On July 22, 2003, we furnished a Form 8-K to the Securities and Exchange Commission with respect to our news release dated July 22, 2003, announcing our results for the three months ended June 30, 2003.

On July 24, 2003, we furnished a Form 8-K to the Securities and Exchange Commission with respect to the transcript of our teleconference on July 22, 2003, relating to the results for the three months ended June 30, 2003.

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.

THE LUBRIZOL CORPORATION

/s/ John R. Ahern

John R. Ahern

Chief Accounting Officer and
Duly Authorized Signatory of
The Lubrizol Corporation

Date: November 6, 2003