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GRACO INC
Form 10-Q/A
May 14, 2001

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15 (d) of the
Securities Exchange Act of 1934

For the quarterly period ended March 30, 2001

Commission File Number: 001-9249

GRACO INC.

(Exact name of Registrant as specified in its charter)

Minnesota

(State of incorporation)

41-0285640

(I.R.S. Employer Identification Number)

88 - 11th Avenue N.E.
Minneapolis, Minnesota

(Address of principal executive offices)

55413

(Zip Code)

(612) 623-6000

(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, and (2) has been subject to such filing requirements for the past 90 days.

Yes X No
----- -----

30,794,894 common shares were outstanding as of May 3, 2001.

GRACO INC. AND SUBSIDIARIES

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Non-employee Director Stock Option Plan, as amended and Restated February 23, 2001	Exhibit 10.1
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PART I

GRACO INC. AND SUBSIDIARIES

Item I. CONSOLIDATED STATEMENTS OF EARNINGS

(Unaudited)

	Thirteen Weeks Ended	
	March 30, 2001	March 31, 2000
	-----	-----
	(In thousands except per share amounts)	
Net Sales	\$109,814	\$122,227
Cost of products sold	54,676	60,098
	-----	-----

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Gross Profit	55,138	62,129
Product development	6,287	5,024
Selling, marketing and distribution	20,672	23,814
General and administrative	7,696	8,644
	-----	-----
Operating Profit	20,483	24,647
Interest expense	450	1,235
Other (income) expense, net	213	437
	-----	-----
Earnings Before Income Taxes	19,820	22,975
Income taxes	6,700	8,000
	-----	-----
Net Earnings	\$ 13,120	\$ 14,975
	=====	=====
Basic Net Earnings Per Common Share	\$.43	\$.49
	=====	=====
Diluted Net Earnings Per Common Share	\$.42	\$.48
	=====	=====

See notes to consolidated financial statements.

GRACO INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Unaudited)
(In thousands)

	March 30, 2001	Dec. 29, 2000
	-----	-----
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 4,682	\$ 11,071
Accounts receivable, less allowances of \$4,800 and \$4,700	83,301	85,836
Inventories	41,177	33,079
Deferred income taxes	11,627	11,574
Other current assets	2,565	2,182
	-----	-----
Total current assets	143,352	143,742
Property, Plant and Equipment:		
Cost	193,942	186,872
Accumulated depreciation	(106,615)	(102,883)
	-----	-----
	87,327	83,989
Other Assets	20,840	10,245

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	\$251,519	\$ 237,976
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities:		
Notes payable to banks	\$ 14,241	\$ 15,713
Current portion of long-term debt	1,050	1,310
Trade accounts payable	12,742	12,899
Salaries, wages & commissions	7,962	14,532
Accrued insurance liabilities	10,925	10,622
Income taxes payable	10,678	4,642
Other current liabilities	20,026	22,123
	-----	-----
Total current liabilities	77,624	81,841
Long-term Debt, less current portion	20,500	18,050
Retirement Benefits and Deferred Compensation	27,106	27,230
Shareholders' Equity:		
Common stock	30,778	20,274
Additional paid-in capital	45,902	39,954
Retained earnings	49,992	50,233
Other, net	(383)	394
	-----	-----
Total shareholders' equity	126,289	110,855
	-----	-----
	\$251,519	\$ 237,976
	=====	=====

See notes to consolidated financial statements.

GRACO INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Thirteen Weeks	
	March 30, 2001	March 31, 2000
	-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES:		(In thousands)
Net Earnings	\$13,120	\$14,975
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	4,240	4,005
Deferred income taxes	(182)	127
Change in:		
Accounts receivable	4,065	(9,733)
Inventories	(5,510)	(4,255)
Trade accounts payable	(358)	1,941

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Salaries, wages and commissions	(6,569)	(3,283)
Retirement benefits and deferred compensation	272	124
Other accrued liabilities	2,832	5,267
Other	(789)	(356)
	-----	-----
	11,121	8,812
	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES:		
Property, plant and equipment additions	(6,203)	(2,968)
Proceeds from sale of property, plant and equipment	45	58
Acquisition of business, net of cash acquired	(15,949)	-
	-----	-----
	(22,107)	(2,910)
	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES:		
Borrowings on notes payable and lines of credit	36,274	47,979
Payments on notes payable and lines of credit	(37,307)	(49,939)
Borrowings on long-term debt	23,000	20,000
Payments on long-term debt	(20,810)	(17,265)
Common stock issued	6,320	6,632
Retirement of common stock	(177)	(15,300)
Cash dividends paid	(3,044)	(2,862)
	-----	-----
	4,256	(10,755)
	-----	-----
Effect of exchange rate changes on cash	341	1,099
	-----	-----
Net increase (decrease) in cash and cash equivalents	(6,389)	(3,754)
Cash and cash equivalents:		
Beginning of year	11,071	6,588
	-----	-----
End of Period	\$ 4,682	\$ 2,834
	=====	=====

See notes to consolidated financial statements.

GRACO INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

- The consolidated balance sheet of Graco Inc. and Subsidiaries (the Company) as of March 30, 2001, and the related statements of earnings and cash flows for the thirteen weeks then ended, have been prepared by the Company without being audited.

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In the opinion of management, these consolidated statements reflect all adjustments (consisting of only normal recurring adjustments) necessary to present fairly the financial position of Graco Inc. and Subsidiaries as of March 30, 2001, and the results of operations and cash flows for all periods presented.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. Therefore, these statements should be read in conjunction with the financial statements and notes thereto included in the Company's 2000 Form 10-K.

The results of operations for interim periods are not necessarily indicative of results that will be realized for the full fiscal year.

2. Major components of inventories were as follows (in thousands):

	Mar. 30, 2001	Dec. 29, 2000
	-----	-----
Finished products and components	\$29,675	\$26,812
Products and components in various stages of completion	21,961	20,153
Raw materials	22,601	19,259
	-----	-----
	74,237	66,224
Reduction to LIFO cost	(33,060)	(33,145)
	-----	-----
	\$41,177	\$33,079
	=====	=====

GRACO INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

3. The Company has three reportable segments; Industrial/Automotive, Contractor and Lubrication. The Company does not identify assets by segment. Sales and operating profit by segment for the thirteen weeks ended March 30, 2001 and March 31, 2000 are as follows (in thousands):

	Mar. 30, 2001	Mar. 31, 2000
	-----	-----
Net Sales		
Industrial/Automotive	\$ 47,649	\$ 56,831
Contractor	49,901	54,481
Lubrication	12,264	10,915
	-----	-----
Total	\$109,814	\$122,227
	=====	=====
Operating Profit		
Industrial/Automotive	\$ 9,394	\$ 12,507

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Contractor	8,620	10,486
Lubrication	2,956	2,316
Unallocated Corporate Expenses	(487)	(662)
	-----	-----
Consolidated Operating Profit	\$ 20,483	\$ 24,647
	=====	=====

4. There have been no changes to the components of comprehensive income from those noted in the 2000 Form 10-K. Total comprehensive income for the quarter was \$12.4 million in 2001 and \$14.2 million in 2000.
5. The adoption of SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" on December 30, 2000, resulted in no transition adjustment. See Note A to financial statements included in the Company's 2000 Form 10-K for a description of the Company's use of derivative instruments and hedging activities.
6. On March 19, 2001, the Company purchased ASM Company, Inc. for \$16 million cash. Based on management's estimates of value, the purchase price has been allocated to net tangible assets of approximately \$5 million and intangible assets totaling approximately \$11 million. Intangible assets are included in the other assets caption on the consolidated balance sheets. The purchase price allocation is subject to adjustment upon completion of an independent appraisal. ASM manufactures and markets spray tips, guns, poles and other accessories for the professional painter. ASM had sales of approximately \$11 million in 2000.

Item 2.

GRACO INC. AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Results of Operations

Net sales and earnings in the first quarter decreased from last year. The impact of reduced sales on net earnings was mitigated by a reduction of expenses. The increase in product development expense was more than offset by reductions in other operating expenses.

The following table sets forth items from the Company's Consolidated Statements of Earnings as percentages of net sales:

	Thirteen Weeks Ended	
	March 30, 2001	March 31, 2000
	-----	-----
Net Sales	100.0%	100.0%
Cost of products sold	49.8	49.2
Product development	5.7	4.1
Selling, marketing and distribution	18.8	19.5
General and administrative	7.0	7.0
	-----	-----
Operating Profit	18.7	20.2
Interest expense	0.4	1.0
Other (income) expense, net	0.2	0.4

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	-----	-----
Earnings Before Income Taxes	18.1	18.8
Income taxes	6.1	6.5
	-----	-----
Net Earnings	12.0%	12.3%
	=====	=====

Net Sales

Net sales in the first quarter of 2001 were down 10 percent from first quarter 2000. Economic conditions in North America led to reduced demand and lower sales in the Industrial / Automotive segment (down 16 percent) and the Contractor Equipment segment (down 8 percent). Lubrication Equipment segment sales (up 12 percent) were helped by new products launched last September and large sales to several key customers. Within the Contractor Equipment segment, sales in the home center channel were \$9.3 million, up 3 percent from the first quarter of 2000. The Company began selling through the home center channel in January 2000, and most of the sales in the first quarter of 2000 were initial stocking orders.

Geographically, sales in the Americas decreased 13 percent. In Europe, sales measured in local currencies increased 2 percent, but decreased 4 percent after unfavorable currency translation. Asia Pacific sales were 3 percent lower than last year, but would have increased 4 percent if translated at consistent exchange rates. Fluctuations in exchange rates adversely impacted consolidated net sales for the quarter by approximately \$2 million.

Gross Profit

Gross profit as a percentage of net sales was 50.2 percent compared to 50.8 percent last year. Gross profit as a percentage of net sales would have decreased only .2 percentage points if sales and cost of products sold were translated at consistent exchange rates.

Operating Expenses

Product development expense increased 25 percent from the first quarter of 2000, as several new products approached launch dates. Other operating expenses decreased commensurate with reduced sales levels. Selling, marketing and distribution expense decreased 13 percent and decreased as a percentage of sales to 18.8 percent from 19.5 percent. First quarter 2000 included significant spending related to the introduction of new products and entry into the home center channel. General and administrative expenses were down 11 percent due to controls placed on spending, including restrictions on discretionary items, and the impact of reduced sales on incentive bonus provisions.

Interest Expense and Other Income (Expense)

Interest expense decreased due to reduced debt levels.

Liquidity and Capital Resources

The Company generated \$11.1 million of cash flow from operating activities in the first three months of 2000, compared to \$8.8 million for the same period last year. Significant uses of cash in 2001 included the acquisition of ASM Company, Inc. and the construction in progress of expanded manufacturing,

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warehouse and office facilities in Minneapolis. In 2000, the Company utilized cash flow to retire \$15.3 million of common stock. The Company plans to expand its Sioux Falls, South Dakota manufacturing facilities to accommodate the move of ASM operations from its current location in California. The Company had unused lines of credit available at March 30, 2001 totaling \$90 million. The available credit facilities and internally generated funds provide the Company with the financial flexibility to meet liquidity needs.

Outlook

The Company remains cautious about its outlook for 2001, as the North American economy has slowed down considerably from the levels of a year ago. Nonetheless, management remains confident that the Company will continue to post good results in light of the circumstances. Management expects to generate incremental revenues and profits by aggressively implementing growth strategies of developing new products, expanding distribution, entering new markets and pursuing strategic acquisitions.

SAFE HARBOR CAUTIONARY STATEMENT

The information in this 10-Q contains "forward-looking statements" about the Company's expectations of the future, which are subject to certain risk factors that could cause actual results to differ materially from those expectations. These factors include economic conditions in the United States and other major world economies, currency exchange fluctuations and additional factors identified in Exhibit 99 to the Company's Report on Form 10-K for fiscal year 2000.

PART II

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

2001 Executive Corporate and SBU Bonus Plan	Exhibit 10
Non-employee Director Stock Option Plan, as amended and restated February 23, 2001	Exhibit 10.1
Computation of Net Earnings per Common Share	Exhibit 11

- (b) No reports on Form 8-K have been filed during the quarter for which this report is filed.

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.

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GRACO INC.

Date: May 1, 2001

By: /s/George Aristides

George Aristides
Chief Executive Officer

Date: May 1, 2001

By: /s/James A. Graner

James A. Graner
Vice President & Controller
("duly authorized officer")