

SECURITIES AND EXCHANGE COMMISSION

FORM 10-Q

Quarterly report pursuant to sections 13 or 15(d)

Filing Date: **1995-06-13** | Period of Report: **1995-04-30**  
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FILER

**VARITRONIC SYSTEMS INC**

CIK: **738633** | IRS No.: **411442400** | State of Incorpor.: **MN** | Fiscal Year End: **0731**  
Type: **10-Q** | Act: **34** | File No.: **000-16566** | Film No.: **95546674**  
SIC: **2670** Converted paper & paperboard prods (no containers/boxes)

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## FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549 QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE  
ACT OF 1934

For the Quarterly Period Ended April 30, 1995

OR

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

Commission File Number: 0-16566

VARITRONIC SYSTEMS, INC.  
(Exact name of registrant as specified in its charter)Minnesota  
(State or other jurisdiction of  
incorporation or organization)41-1442400  
(I.R.S. Employer  
Identification No.)300 Interchange North  
300 Highway 169 South  
Minneapolis, Minnesota  
(Address of principal executive offices)55426  
(Zip Code)612-542-1500  
(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  NoOn June 9, 1995 there were 2,326,820 shares of the registrant's \$.01 par value  
common stock outstanding.

## PART I - FINANCIAL INFORMATION

## Item 1: Financial statements

VARITRONIC SYSTEMS, INC.

CONSOLIDATED BALANCE SHEETS  
ASSETS<TABLE>  
<CAPTION>

	(UNAUDITED) APRIL 30, 1995 <C>	JULY 31, 1994 <C>
<S>		
Current assets:		
Cash	\$ 299,151	\$ 209,844
Accounts receivable, net	9,599,982	8,902,523
Inventories:		
Finished goods	4,423,525	4,935,609
Raw materials and component parts	8,650,422	6,801,194
Total inventories	13,073,947	11,736,803

Other current assets	1,114,983	826,322
Total current assets	24,088,063	21,675,492
Property and equipment, net	4,699,754	4,264,098
Total assets	\$28,787,817	\$25,939,590

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities:		
Borrowings under line of credit	\$ 5,200,000	\$ 3,000,000
Accounts payable	3,004,046	2,992,734
Accrued liabilities	1,054,595	1,216,335
Total current liabilities	9,258,641	7,209,069
Stockholders' equity:		
Common stock, \$.01 par value, 10,000,000 shares authorized; 2,326,820 and 2,408,123 shares issued and outstanding	23,268	24,081
Additional paid-in capital	207,391	-
Retained earnings	19,298,517	18,706,440
Total stockholders' equity	19,529,176	18,730,521
Total liabilities and stockholders' equity	\$28,787,817	\$25,939,590

</TABLE>

See accompanying notes to unaudited consolidated financial statements

VARITRONIC SYSTEMS, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS  
(UNAUDITED)

<TABLE>  
<CAPTION>

	THREE MONTHS ENDED APRIL 30,		NINE MONTHS ENDED APRIL 30,	
	1995	1994	1995	1994
<S> Net sales	<C> \$12,331,941	<C> \$11,064,181	<C> \$36,318,384	<C> \$33,308,474
Cost of sales	8,088,160	6,830,351	23,215,886	20,419,493
Gross margin	4,243,781	4,233,830	13,102,498	12,888,981
Operating expenses:				
Marketing and sales	1,733,541	1,721,606	4,727,016	5,059,298
General and administrative	1,330,129	1,577,761	4,004,224	4,492,693
Product development	752,395	515,569	1,893,536	1,684,736
Total operating expenses	3,816,065	3,814,936	10,624,776	11,236,727
Income from operations	427,716	418,894	2,477,722	1,652,254
Other income	801	381	8,693	1,164
Interest expense	(80,941)	(29,393)	(233,485)	(38,159)
Income before income taxes	347,576	389,882	2,252,930	1,615,259
Provision for income taxes	110,000	125,000	740,000	550,000
Net income	\$ 237,576	\$ 264,882	\$ 1,512,930	\$ 1,065,259
Net income per share	\$.10	\$.10	\$.65	\$.40

Weighted average common shares outstanding	2,325,000	2,625,000	2,318,000	2,657,000
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</TABLE>

See accompanying notes to unaudited consolidated financial statements

VARITRONIC SYSTEMS, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)

<TABLE>  
<CAPTION>

<S>	NINE MONTHS ENDED APRIL 30,	
	<C> 1995	<C> 1994
OPERATING ACTIVITIES:		
Net income	\$ 1,512,930	\$ 1,065,259
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,247,648	857,735
Provision for inventory valuation allowance	125,000	25,000
Provision for uncollectible accounts receivable	48,820	234,168
Changes in operating assets and liabilities:		
Accounts receivable	(746,279)	(433,953)
Inventories	(1,462,144)	(699,858)
Other current assets	(288,661)	(160,588)
Accounts payable	11,312	655,074
Accrued liabilities	(161,740)	(298,504)
Net cash provided by operating activities	286,886	1,244,333
INVESTING ACTIVITIES:		
Additions to property and equipment	(1,683,304)	(2,099,405)
Net cash used by investing activities	(1,683,304)	(2,099,405)
FINANCING ACTIVITIES:		
Borrowings under line of credit	5,200,000	4,500,000
Repayments under line of credit	(3,000,000)	(2,500,000)
Repurchase of common stock	(921,969)	(1,281,000)
Proceeds from sale of common stock under incentive stock option plan and employee stock purchase plan	207,694	163,282
Net cash provided by financing activities	1,485,725	882,282
Net increase in cash	89,307	27,210
CASH AT BEGINNING OF PERIOD	209,844	334,728
CASH AT END OF PERIOD	\$ 299,151	\$ 361,938

</TABLE>

See accompanying notes to unaudited consolidated financial statements

VARITRONIC SYSTEMS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)

1. Consolidated Financial Statements:

The unaudited consolidated financial statements as of April 30, 1995, and for the three and nine months then ended, reflect, in the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly the financial position and results of operations for the interim periods. The unaudited consolidated interim financial statements should be read in conjunction with the consolidated financial statements and notes thereto contained in the Company's report on Form 10-K for the year ended July 31, 1994.

## 2. Share Repurchase:

The Board of Directors approved a resolution at its May 16, 1995 meeting authorizing the Company to purchase up to 300,000 shares of its common stock on the open-market or in privately negotiated transactions.

## ITEM 2.

### MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

#### RESULTS OF OPERATIONS:

Net sales increased to \$12,332,000 in the third quarter of fiscal 1995 compared to net sales of \$11,064,000 in the year-ago period, an increase of \$1,268,000 or 11.5 percent. Machine sales increased by 19.8 percent and supply sales increased by 6.7 percent from the year-ago third quarter. Sales of the PosterPrinter™ product line increased by 20.6 percent from the third quarter of fiscal 1994, and represented 36.7 percent of current quarter net sales. Approximately 75 percent of PosterPrinter machines sold domestically were equipped with a ProLynx™ computer interface. The ProImage PosterPrinter machines sold with a ProLynx retail for \$3,995, compared to a \$3,495 retail price for machines sold without a ProLynx. The Company launched the EasyStep™ 2500 labeling machine, the industrial market version of the ProPartner™, in the current year third quarter. Sales of the EasyStep 2500/ProPartner product line were approximately \$800,000 in the current quarter. EasyStep 4000 product line sales increased by 7.5 percent from the third quarter of a year ago, and represented 24.5 percent of current quarter sales, despite a significant decrease in sales of EasyStep 4000 supplies to a major distributor due to a change in the distributor's inventory management policy. The Company expects sales of EasyStep 4000 supplies to return to the levels of prior quarters in the fourth quarter of fiscal 1995. International sales increased by 58.4 percent from the third quarter of fiscal 1994 due to increases in EasyStep 4000 and PosterPrinter product line sales.

The Company announced a new product, the VintageColor™ printing system in the current year third quarter. The Company exhibited the printing system at a domestic trade show in March, and at a European trade show in early May. The VintageColor is a wide format, full-color printing system which produces output in 24 or 36 inch widths up to 100 feet long. The VintageColor system includes an inkjet printer, raster image processor software, and other options including a pre-configured color server, color calibrated scanners and a variety of print media and inks. The Company expects sales of this product in the fourth quarter of the current fiscal year.

Net sales for the nine months ended April 30, 1995 were \$36,318,000 compared to net sales of \$33,308,000 for the nine months ended April 30, 1994, an increase of \$3,010,000, or 9.0 percent. Sales of the EasyStep 4000 product line increased by 38.2 percent from last year, while sales of the PosterPrinter product line increased by 19.5 percent between the comparable periods. International sales of these two product lines increased significantly between the nine month periods resulting in a 22.3 percent increase in international sales for the nine month comparative periods. Current year nine month sales of the EasyStep 2500/ProPartner product line, launched during the current fiscal year, were \$1,386,000. Sales of the Company's mature product lines decreased by 23.7 percent from the year-ago period. This decrease is consistent with Company expectations.

Gross margin was 34.4 percent and 36.1 percent for the quarter and nine months ended April 30, 1995 compared to 38.3 percent and 38.7 percent in the comparable periods last year. In the current quarter, overall production volumes declined due to the short-term volume adjustment for the EasyStep 4000 supply sales as noted above. The decreased production levels resulted in unabsorbed burden and direct labor costs which increased cost of goods sold. Machine margins decreased from last year due to lower margins on PosterPrinter machine sales. PosterPrinter machines and supplies are imported from Japan, and are purchased using Japanese yen. On a year-to-year comparison, the decreased value of the U.S. dollar against the yen increased the cost of these imported products. The current dollar weakness against the yen will further increase the cost of these products in the future. The Company enters into foreign exchange contracts to hedge inventory purchase commitments denominated in Japanese yen. Supply margins were consistent for all of the comparable periods.

Operating expenses were \$3,816,000 and \$10,625,000 in the current quarter and nine month period, respectively, compared to \$3,815,000 and \$11,237,000 for the comparable periods in the prior year. Overall marketing and sales expenses were

comparable from the year-ago quarterly level. However, media and promotional expenses decreased as the Company changed its promotional and advertising programs. These expense reductions were offset by costs incurred to introduce the Company's newest product, the VintageColor printing system. General and administrative expenses decreased by \$248,000 in the current year third quarter compared to the third quarter last year. The prior year third quarter included a bad debt provision of \$237,000 due to the bankruptcy filing of a major domestic dealer. Current quarter product development expenses increased to \$752,000 from \$516,000 one year ago primarily related to supply development projects and software development for the new VintageColor printing system. Operating expenses for the nine month period decreased by \$612,000 from the year ago levels. In addition to the items noted above, prior year operating expenses included \$250,000 incurred in connection with acquisition discussions with Kroy, Inc. which were terminated in December 1993. These costs were included in general and administrative expenses.

Interest expense totaled \$81,000 for the current quarter, and \$233,000 for the current nine month period. Current year average daily borrowings under the Company's \$10,000,000 revolving line of credit were approximately \$3,853,000.

The Company provided for income taxes at a 31.6 percent and 32.8 percent rate for the current quarter and nine months compared to an effective tax rate of 32.1 percent for fiscal 1994. The current period tax rate includes an increased benefit from the research and experimentation tax credit.

#### LIQUIDITY AND CAPITAL RESOURCES:

Cash was \$299,000 at April 30, 1995 compared to \$210,000 at July 31, 1994. Cash provided by operations was \$287,000 for the current nine month period compared to cash provided by operations of \$1,244,000 last year. The decrease in the current year was due to several items including an increase in inventory of \$1,337,000 which was comprised mainly of the EasyStep 4000 and the EasyStep 2500/ProPartner product lines. Accounts receivable increased due to an increase in international receivables which are generally given longer payment terms. Cash provided by operating activities also included an increase in net income of \$448,000, and an increase in non-cash items of \$305,000. Property and equipment additions under investing activities were \$1,683,000 compared to \$2,099,000 last year. Current year additions included leasehold improvements, furniture and fixtures for a new leased facility which houses personnel working on the VintageColor and PosterPrinter products. There were also fixed asset additions for test and training equipment to support the new product. Prior year fixed asset additions were mainly specialized tooling for the EasyStep 2500/ProPartner product line. Net cash provided by financing activities was \$1,486,000 in the current year compared to \$882,000 in last year's nine month period. Under its \$10,000,000 bank line of credit, the Company increased its bank borrowings to \$5,200,000 at April 30, 1995 from \$3,000,000 at July 31, 1994. These borrowings were used to finance the increase in accounts receivable and inventory, to purchase fixed assets, and to repurchase shares of the Company's stock under its prior share repurchase program. As of April 30, 1995, working capital increased to \$14,829,000 from \$14,466,000 at July 31, 1994, and the current ratio was 2.6 to 1 compared to 3.0 to 1 at July 31, 1994. The decrease in the current ratio resulted from increased bank borrowings used to repurchase Company shares and purchase fixed assets.

The Company believes it can continue to finance its working capital, share repurchase and capital expenditure needs for the foreseeable future from internally generated funds and its available bank line of credit.

#### DISTRIBUTION RIGHTS:

The Company has exclusive distribution rights in the United States, Canada, Mexico and certain South American countries for the ProImage PosterPrinter under a distribution agreement with Itochu Corporation (a Japanese trading company). The Company has met the minimum order requirements under the agreement and continues to maintain exclusive distribution rights in the noted countries. The distribution agreement expires December 31, 1995. The Company has non-exclusive distribution for the 220 volt ProImage in certain international countries, primarily in Europe, under a letter agreement with Itochu. This letter agreement incorporates by reference substantially all of the terms and conditions of the exclusive distribution agreement referred to above.

#### PART II - OTHER INFORMATION

Item 6. Exhibits and Reports on Form 8-K

- (a) Exhibits: Exhibit 27 - Financial Data Schedule (For SEC use only).
  
- (b) Reports on Form 8-K: No reports on Form 8-K have been filed during the quarter.

SIGNATURE

Pursuant to the requirements of Section 13 or 15(d) 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.

Date: June 9, 1995

VARITRONIC SYSTEMS, INC.

/s/ Norbert F. Nicpon  
Norbert F. Nicpon  
Vice President of Finance and  
Administration and Chief  
Financial Officer

<TABLE> <S> <C>

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