A C MOORE ARTS & CRAFTS INC
Form 10-Q
August 13, 2001

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington D.C. 20549

FORM 10-Q

(Mark One)
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2001
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: 000-23157

A.C. MOORE ARTS & CRAFTS, INC.
(Exact name of registrant as specified in its charter)

Pennsylvania	22-3527763
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

500 University Court, Blackwood, NJ 08012
(Address of principal executive offices)
(Zip Code)

(856) 228-6700
(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 the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Class	Outstanding at August 8, 2001
Common Stock, no par value	7,434,264

A.C. MOORE ARTS & CRAFTS, INC.

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A.C. MOORE ARTS & CRAFTS, INC.
CONSOLIDATED BALANCE SHEETS
(dollars in thousands)

	June 30, 2001 (unaudited)
ASSETS	
Current assets:	
Cash and cash equivalents	$ 4,016
Inventories	82,921

Prepaid expenses and other current assets	2,316
	89,253
Property and equipment, net	24,000
Other assets	799
	$ 114,052
LIABILITIES AND SHAREHOLDERS' EQUITY	
Current liabilities:	
Short-term debt	$ 17,500
Current portion of capital leases	1,260
Accounts payable to trade and others	18,135
Accrued payroll and payroll taxes	2,197
Accrued expenses	3,630
Income taxes payable	143
	42,865
Long-term liabilities:	
Capital leases	2,540
Deferred taxes	2,320
Other long-term liabilities	2,863
	7,723
	50,588
SHAREHOLDERS' EQUITY	
Preferred stock, no par value, 5,000,000 shares authorized, none issued	
Common stock, no par value, 20,000,000 shares authorized, 7,428,833 shares outstanding at June 30, 2001 and 7,415,333 outstanding at December 31, 2000	43,345
Retained earnings	20,119
	63,464
	$ 114,052

See accompanying notes to financial statements

A.C. MOORE ARTS & CRAFTS, INC.
CONSOLIDATED STATEMENTS OF INCOME
(dollars in thousands, except per share data)
(unaudited)

Three months ended

	June 30,	
	2001	2000
Net sales	$ 67,132	$ 55,186
Cost of sales (including buying and distribution costs)	42,265	34,919
Gross margin	24,867	20,267
Selling, general and administrative expenses	24,718	19,920
Pre-opening expenses	374	311
Income (loss) from operations	(225)	36
Net interest expense (income)	149	12
Income (loss) before income taxes	(374)	24
Income tax expense (benefit)	(142)	9
Net income (loss)	$ (232)	$ 15
Basic net income (loss) per share	$ (0.03)	$ 0.00
Weighted average shares outstanding	7,428,833	7,405,000
Diluted net income (loss) per share	$ (0.03)	$ 0.00
Weighted average shares outstanding plus impact of stock options	7,428,833	7,435,000

See accompanying notes to financial statements

A.C. MOORE ARTS & CRAFTS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(dollars in thousands)
(unaudited)

	Six M
	2001
Cash flows from operating activities:	
Net Income (loss)	$ (294)
Adjustments to reconcile net income (loss) to net cash (used in) operating activities:	
Depreciation and amortization	2,357

Compensation expense related to stock options	-
Changes in assets and liabilities:	
Inventories	(10,135)
Prepaid expenses and other current assets	(264)
Accounts payable, accrued payroll payroll taxes and accrued expenses	(10,371)
Income taxes payable	(3,115)
Other long-term liabilities	264
Other	(72)
Net cash (used in) operating activities	(21,630)
Cash flows (used in) investing activities: Capital expenditures	(4,840)
Cash flows from financing activities:	
Proceeds from bank overdraft	-
Proceeds from line of credit	17,500
Exercise of stock options	77
Proceeds from capital leases	2,791
Repayment of capital leases	(192)
Net cash provided by financing activities	20,176
Net (decrease) in cash	(6,294)
Cash and cash equivalents at beginning of period	10,310
Cash and cash equivalents at end of period	$ 4,016

See accompanying notes to financial statements

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

(1) Basis of Presentation

The consolidated financial statements included herein include the accounts of A.C. Moore Arts & Crafts, Inc. and its wholly owned subsidiaries (collectively the "Company"). The Company is a chain of 55 retail stores selling arts and crafts merchandise. The stores are located throughout the Eastern United States.

These financial statements have been prepared by management without audit and should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2000. Due to the seasonality of the Company's business, the results for the interim periods are not necessarily indicative of the results for the year. The accompanying consolidated financial statements reflect, in the opinion of management, all adjustments necessary for a fair presentation of the interim financial statements. In the opinion of management, all such adjustments are of a normal and recurring nature.

(2) Management Estimates

The preparation of these consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of expenses during the reported period and related disclosures. Significant estimates made as of and for the three and six month periods ended June 30, 2001 and 2000 include provisions for shrinkage, capitalized buying, warehousing and distribution costs related to inventory and markdowns of merchandise inventories. Actual results could differ materially from those estimates.

(3) Earnings Per Share

The weighted average shares outstanding plus impact of stock options for the three and six month periods ended June 30, 2001 excludes potentially dilutive shares as the result would be antidilutive.

(4) New Accounting Standard

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards ("SFAS") No. 133, Accounting for Derivative Instruments and Hedging Activities, which requires that all derivative financial instruments be recognized as either assets or liabilities in the balance sheet. SFAS No. 133, which was effective for the Company's first quarter of 2001, has not had a material impact on the Company's consolidated results of operation, financial position or cash flows.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis contains certain forward-looking statements. These forward-looking statements do not constitute historical facts and involve risks and uncertainties. Actual results could differ materially from those referred to in the forward-looking statements due to a number of factors, including, but not limited to, the following: customer demand, the effect of economic conditions, the impact of competitors' locations or pricing, the availability of acceptable real estate locations for new stores, difficulties with respect to new information system technologies, supply constraints or difficulties, the effectiveness of advertising strategies and the ability to meet capital needs. For additional information concerning factors that could cause actual results to differ materially from the information contained herein, reference is made to the information under the heading "Cautionary Statement Relating to Forward Looking Statements" in the Company's Annual Report on Form 10-K as filed with the Securities and Exchange Commission.

Due to the importance of the fall selling season, the fourth quarter has historically contributed, and the Company expects it will continue to contribute, disproportionately to the Company's profitability for the entire year. As a result, the Company's quarterly results of operations may fluctuate. In addition, results of a period shorter than a full year may not be indicative of results expected for the entire year.

Results of Operations

The following table sets forth, for the periods indicated, selected statement of

operations data expressed as a percentage of net sales and the number of stores open at the end of each such period:

	Three months ended June 30,		
	2001	2000	20
Net sales	100.0%	100.0%	100
Cost of sales	63.0%	63.3%	63
Gross margin	37.0%	36.7%	36
Selling, general and administrative expenses	36.8%	36.1%	36
Store pre-opening expenses	0.5%	0.6%	1
Income (loss) from operations	(0.3)%	0.0%	(0
Net interest expense (income)	0.2%	0.0%	0
Income (loss) before income taxes	(0.5)%	0.0%	(0
Income tax expense (benefit)	(0.2)%	0.0%	(0
Net income (loss)	(0.3)%	0.0%	(0
Number of stores open at end of period	55	45	

Three Months Ended June 30, 2001 Compared to Three Months Ended June 30, 2000

Net Sales. Net sales increased $11.9 million, or 21.6%, to $67.1 million in the three months ended June 30, 2001 from $55.2 million in the comparable 2000 period. This increase resulted from (i) net sales of $4.2 million from five new stores opened in 2001, (ii) net sales of $5.3 million from stores opened in 2000 not included in the comparable store base, and (iii) a comparable store sales increase of $2.4 million, or 4%. Stores are added to the comparable store base at the beginning of the fourteenth full month of operation.

Gross Margin. Cost of sales includes the cost of merchandise, plus certain distribution and purchasing costs. Cost of sales increased $7.3 million, or 21%, to $42.3 million in the three months ended June 30, 2001 from $34.9 million in the three months ended June 30, 2000. The gross margin increased $4.6 million, or 22.7%, to $24.9 million in the three months ended June 30, 2001 from $20.3 million in the three months ended June 30, 2000. The gross margin increased to 37.0% of net sales in the three months ended June 30, 2001 from 36.7% in the three months ended June 30, 2000. The increase is due to cost reductions achieved from our vendors and leveraging of our buying and distribution expense, offset by higher freight costs.

Selling, General and Administrative Expenses. Selling, general and administrative expenses include (a) direct store level expenses, including rent and related operating costs, payroll, advertising, depreciation and other direct

costs, and (b) corporate level costs not directly associated with or allocable to cost of sales including executive salaries, accounting and finance, corporate information systems, office facilities and other corporate expenses. Selling, general and administrative expenses increased $4.8 million, or 24.1%, in the three months ended June 30, 2001 to $24.7 million from $19.9 million in the three months ended June 30, 2000. Of the increase, $3.7 million was attributable to the stores opened in 2001 which were not open during 2000 and the stores opened in 2000 not in the comparable store base. Of the remainder, $800,000 is due to increases in the comparable stores and $300,000 is attributable to the increase in corporate costs to support the growth of the Company. As a percentage of sales, selling, general and administrative costs increased to 36.8% of net sales in the three months ended June 30, 2001 from 36.1% of net sales in the three months ended June 30, 2000. This increase is primarily due to newer stores, which, on average, have higher operating costs as a percent of sales than older stores.

Store Pre-Opening Expenses. The Company expenses store pre-opening expenses as incurred. Pre-opening expense for the two new stores opened in the second quarter of 2001, the new store which opened in July and one store which was relocated amounted to $374,000. In the second quarter of 2000, the Company incurred store pre-opening costs of $311,000 related to the three stores opened in that quarter.

Net Interest Expense (Income). In the second quarter of 2001, the Company had net interest expense of $149,000 compared with interest expense of $12,000 in 2000. The change is due to the use of short-term borrowing to fund the new stores added in 2000 and 2001.

Income Taxes. The Company's effective income tax rate was 38.0% for both the second quarters ended June 30, 2001 and June 30, 2000.

Six Months Ended June 30, 2001 Compared to Six Months Ended June 30, 2000.

Net Sales. Net sales increased $25.6 million, or 23.7%, to $133.6 million in the six months ended June 30, 2001 from $108.0 million in the comparable 2000 period. This increase resulted from (i) net sales of $6.5 million from five new stores opened in 2001, (ii) net sales of $14.9 million from stores opened in 2000 not included in the comparable store base, and (iii) a comparable store sales increase of $4.2 million, or 4%.

Gross Margin. Cost of sales increased $15.9 million, or 23.4%, to $84.2 million in the six months ended June 30, 2001 from $68.3 million in the six months ended June 30, 2000. The gross margin increased $9.6 million, or 24.3%, to $49.3 million in the six months ended June 30, 2001 from $39.7 million in the six months ended June 30, 2000. The gross margin increased to 36.9% of net sales in the six months ended June 30, 2001 from 36.7% in the six months ended June 30, 2000.

Selling, General and Administrative Expenses. Selling, general and administrative expenses increased $9.6 million, or 25.0% in the six months ended June 30, 2001 to $48.2 million from $38.5 million in the six months ended June 30, 2000. Of the increase, $7.6 million was attributable to the stores opened in 2001 which were not open during 2000 and the stores opened in 2000 not in the comparable store base. Of the remainder, $1.2 million is due to increases in the comparable stores and $800,000 is attributable to the increase in corporate costs to support the growth of the Company. As a percentage of sales, selling, general and administrative costs increased to 36.0% of net sales in the six months ended June 30, 2001 from 35.6% of net sales in the six months ended June

30, 2000. This increase is primarily due to the newer stores which, on average, have higher operating costs as a percent to sales than older stores.

Store Pre-Opening Expenses. Pre-opening expense for the five new stores opened in the first half of 2001, the new store which opened in July and two stores which were relocated during the period amounted to $1.4 million. In the first six months of 2000 the Company opened five new stores and incurred pre-opening expenses of $956,000.

Net Interest Expense (Income). In the first six months of 2001 the Company had net interest expense of $181,000 compared with interest income of $54,000 in 2000. The change is due to the use of short term borrowing to fund the new stores added in 2000 and 2001.

Income Taxes. The Company's effective income tax rate was 38.0% for both the six month periods ended June 30, 2001 and June 30, 2000.

Liquidity and Capital Resources

The Company's cash needs are primarily for working capital to support its inventory requirements and capital expenditures, store pre-opening costs and beginning inventory for new stores.

At June 30, 2001 and December 31, 2000 the Company's working capital was $46.4 million and $47.2 million, respectively. Cash used in operations was $21.6 million for the six months ended June 30, 2001 primarily as a result of the seasonal reduction of accounts payable and accrued liabilities in the amount of $10.4 million, payments for income taxes of $3.1 million and an increase in inventory of $10.1 million to support the new stores and as a result of accelerating the receipt of product for the fall and Christmas seasons.

Net cash used in investing activities during the six months ended June 30, 2001 was $4.8 million. This use of cash was for capital expenditures, primarily related to new stores. In 2001, the Company expects to spend approximately $11.0 million on capital expenditures, which includes approximately $9.0 million for new store openings, and the remainder for remodeling and systems in existing stores, warehouse equipment and systems development. There are no other material commitments for capital expenditures other than new store openings in the next 12 months.

Net cash provided by financing activities includes $17.5 million in borrowings under the Company's $25 million revolving credit facility and $2.8 million of proceeds from capital leases. The proceeds were used to fund new store openings, including related capital expenditures.

On August 3, 2001 the Company signed a new $50 million three year revolving credit agreement with KeyBank, agent, and First Union National Bank. Borrowings under the credit agreement will bear interest rates that will vary between LIBOR plus 150 basis points and LIBOR plus 200 basis points, depending on the fixed charge coverage ratio. The Company believes the cash generated from operations during the year and available borrowings under the new financing agreement will be sufficient to finance its working capital and capital expenditure requirements for at least the next 12 months.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Not Applicable.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Not Applicable.

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not Applicable.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Company held its Annual Meeting of Shareholders on May 17, 2001. At the meeting, shareholders elected two Class A directors to hold office for a term of three years until their successors are duly elected and qualified. The nominees for director received the following votes at the meeting.

	For	Withhold Authority
Richard J. Bauer	6,925,583	21,860
Richard J. Drake	6,920,668	26,775

The term of office for each of the following directors continued after the meeting: William Kaplan, John E. (Jack) Parker, Patricia A. Parker and Richard Lesser.

ITEM 5. OTHER INFORMATION

Not Applicable.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits:

+ 10.8 Employment Agreement, dated June 4, 2001, between Rex A. Rambo and A.C. Moore, Inc.

+ 10.9 Employment Agreement, dated June 11, 2001, between Lawrence H. Fine and A.C. Moore, Inc.

10.10 Credit Agreement, dated as of August 3, 2001, among A.C. Moore Incorporated, The Lenders Party Thereto, and KeyBank National Association, as Administrative Agent and Lead Arranger.

10.11 Security Agreement, dated as of August 3, 2001, among A.C. Moore Incorporated, A.C. Moore Arts & Crafts, Inc., Moorestown Finance, Inc., Blackwood Assets, Inc., each of A.C. Moore Incorporated's subsidiaries, and KeyBank National Association.

10.12 Guarantee Agreement, dated as of August 3, 2001, among A.C. Moore Arts & Crafts, Inc., A.C. Moore Incorporated, Moorestown Finance, Inc., Blackwood Assets, Inc., each of

the subsidiaries of A.C. Moore Incorporated listed in Schedule 1 to the Guarantee Agreement, and KeyBank National Association.

(b) There were no reports on Form 8-K filed during the quarter ended June 30, 2001.

+ Management Contract or compensatory plan or arrangement.

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.

A.C. MOORE ARTS & CRAFTS, INC.

Date: August 10, 2001 By: /s/ Leslie H. Gordon

Executive Vice President and Chief Financial Officer(duly authorized officer and principal financial officer)

EXHIBIT INDEX

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