

Edgar Filing: MONDAVI ROBERT CORP - Form 10-Q

MONDAVI ROBERT CORP  
Form 10-Q  
May 15, 2002

U.S. 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 31, 2002

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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: 33-61516  
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THE ROBERT MONDAVI CORPORATION

Incorporated under the laws  
of the State of California

I.R.S. Employer Identification:  
94-2765451

Principal Executive Offices:  
7801 St. Helena Highway  
Oakville, CA 94562  
Telephone: (707) 259-9463

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  
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As of April 30, 2002, there were issued and outstanding 9,353,613 shares of the issuer's Class A Common Stock and 6,852,647 shares of the issuer's Class B Common Stock.

PART I

Item 1. Financial Statements.

THE ROBERT MONDAVI CORPORATION  
CONSOLIDATED BALANCE SHEETS  
(In thousands, except share data)

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ASSETS

	March 31 2002 ----- Unaudite
Current assets:	
Cash and cash equivalents	\$ -
Accounts receivable--trade, net	79,408
Inventories	417,110
Prepaid expenses and other current assets	11,623
	-----
Total current assets	508,141
Property, plant and equipment, net	324,640
Investments in joint ventures	32,193
Other assets	13,524
	-----
Total assets	\$ 878,498 =====

LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities:	
Book overdraft	\$ 3,157
Notes payable to banks	3,100
Accounts payable--trade	18,221
Employee compensation and related costs	11,760
Other accrued expenses	14,168
Current portion of long-term debt	12,641
	-----
Total current liabilities	63,047
Long-term debt, less current portion	363,446
Deferred income taxes	23,658
Deferred executive compensation	5,321
Other liabilities	3,608
	-----
Total liabilities	459,080
Commitments and contingencies	
Shareholders' equity:	
Preferred Stock:	
Authorized--5,000,000 shares; issued and outstanding--no shares	-
Class A Common Stock, without par value:	
Authorized--25,000,000 shares;	
issued and outstanding--9,296,363 and 9,151,217 shares	92,861
Class B Common Stock, without par value:	
Authorized--12,000,000 shares;	
issued and outstanding--6,852,647 and 6,885,717 shares	11,006
Paid-in capital	11,166
Retained earnings	307,758
Accumulated other comprehensive income:	
Cumulative translation adjustment	(3,352)
Forward contracts	(21)
	-----
Total liabilities and shareholders' equity	\$ 878,498 =====

See Notes to Consolidated Financial Statements.

THE ROBERT MONDAVI CORPORATION  
CONSOLIDATED STATEMENTS OF INCOME  
(Unaudited) (in thousands, except per share data)

	Three Months Ended March 31,		Nine
	2002	2001	2002
	----	----	----
Gross revenues	\$109,833	\$117,665	\$332,434
Less excise taxes	5,543	5,584	16,130
	-----	-----	-----
Net revenues	104,290	112,081	316,304
Cost of goods sold	57,981	60,571	178,300
	-----	-----	-----
Gross profit	46,309	51,510	138,004
Selling, general and administrative expenses	29,429	31,166	93,043
Special charges	- -	- -	12,240
	-----	-----	-----
Operating income	16,880	20,344	32,721
Other income (expense):			
Interest	(5,877)	(6,187)	(16,440)
Equity income from joint ventures	1,137	244	8,936
Other	(7)	56	(643)
	-----	-----	-----
Income before income taxes	12,133	14,457	24,574
Provision for income taxes	4,550	5,566	9,215
	-----	-----	-----
Net income	\$ 7,583	\$ 8,891	\$ 15,359
	=====	=====	=====
Earnings per share-Basic	\$ .47	\$ .56	\$ .96
	=====	=====	=====
Earnings per share-Diluted	\$ .46	\$ .54	\$ .94
	=====	=====	=====
Weighted average number of shares outstanding-Basic	16,093	15,970	16,056
	=====	=====	=====
Weighted average number of shares outstanding-Diluted	16,394	16,428	16,367
	=====	=====	=====

See Notes to Consolidated Financial Statements.

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THE ROBERT MONDAVI CORPORATION  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited, in thousands)

	Nine
	2002
	-----
Cash flows from operating activities:	
Net income	\$ 15,359
Adjustments to reconcile net income to net cash used in operating activities:	
Deferred income taxes	(4,685)
Depreciation and amortization	16,931
Equity income from joint ventures	(8,936)
Special charges and asset write-downs	14,070
Other	367
Changes in assets and liabilities, net of acquisitions:	
Accounts receivable--trade	25,147
Inventories	(62,108)
Other assets	3,874
Accounts payable--trade and accrued expenses	(17,322)
Deferred executive compensation	193
Other liabilities	(159)
	-----
Net cash used in operating activities	(17,269)
	-----
Cash flows from investing activities:	
Acquisitions of property, plant and equipment	(26,109)
Proceeds from sale of assets	12,327
Business acquisition	-
Distributions from joint ventures	9,792
Contributions to joint ventures	(1,128)
	-----
Net cash used in investing activities	(5,118)
	-----
Cash flows from financing activities:	
Book overdraft	3,157
Net additions under notes payable to banks	25,100
Proceeds from issuance of long-term debt	-
Principal repayments of long-term debt	(13,506)
Proceeds from issuance of Class A Common Stock	273
Exercise of Class A Common Stock options	1,321
Other	(1,147)
	-----
Net cash provided by financing activities	15,198
	-----
Net decrease in cash and cash equivalents	(7,189)
Cash and cash equivalents at the beginning of the period	7,189
	-----
Cash and cash equivalents at the end of the period	\$ -
	=====

See Notes to Consolidated Financial Statements.

THE ROBERT MONDAVI CORPORATION  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
 (Dollars in thousands)

NOTE 1 BASIS OF PRESENTATION

In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments (which include only normal recurring adjustments) necessary to present fairly the Company's financial position at March 31, 2002, its results of operations for the three and nine month periods ended March 31, 2002 and 2001 and its cash flows for the nine month periods ended March 31, 2002 and 2001. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted from the accompanying consolidated financial statements. For further information, reference should be made to the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K (the 10-K) for the fiscal year ended June 30, 2001, on file at the Securities and Exchange Commission. Certain fiscal 2001 balances have been reclassified to conform with current year presentation.

Effective July 1, 2001, the Company implemented new pronouncements issued by the Financial Accounting Standards Board's Emerging Issues Task Force that require certain sales incentives and fees paid to retailers to be recorded as reductions of revenue. The Company previously reported these expenses as selling, general and administrative expenses. Prior period financial statements have been restated to reflect this change in classification. The restatement resulted in a \$5,908 and \$16,449 decrease in both revenues and selling, general and administrative expenses for the three and nine months ended March 31, 2001, respectively.

NOTE 2 INVENTORIES

Inventories consist of the following:

	March 31, 2002	June 30, 2001
	----	----
	Unaudited	
Wine in production	\$ 281,939	\$ 226,214
Bottled wine	122,503	109,674
Crop costs and supplies	12,668	22,868
	-----	-----
	\$ 417,110	\$ 358,756
	=====	=====

Inventories are valued at the lower of cost or market and inventory costs are determined using the first-in, first-out (FIFO) method. Costs associated with growing crops are recorded as inventory and are recognized as wine inventory costs in the year in which the related crop is harvested. Included in inventory at March 31, 2002, was \$7,367 of inventory cost step-up remaining from applying purchase accounting to the acquisition of Arrowood.

NOTE 3 DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

The Company has only a limited involvement with derivative instruments and does

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not use them for trading purposes. Forward exchange contracts, generally with average maturities of less than one year, are used as protection against the risk that the eventual U.S. dollar cash flows resulting from certain unrecognized firm purchase commitments and forecasted transactions denominated in foreign currencies will be adversely affected by changes in exchange rates. The derivative financial instruments associated with unrecognized firm purchase commitments are designated as fair-value hedges. The derivative financial instruments associated with forecasted transactions are designated as cash-flow hedges.

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At March 31, 2002, the Company had outstanding forward exchange contracts, hedging primarily European euro purchases of barrels and corks and forecasted receipts of Canadian dollars and European euros, with notional amounts totaling \$10,732. Using exchange rates outstanding as of March 31, 2002, the U.S. dollar equivalent of the contracts totaled \$10,504.

#### NOTE 4 OPERATIONAL CHANGES

During the first quarter of fiscal 2002, the Company implemented a number of operational changes aimed at improving its competitiveness in the slowing economy. These included changes in the Company's Disney California Adventure project and the write-down of certain inventories and fixed assets due to lowered volume growth expectations.

The Company changed from an operator to a sponsor role at Disney's California Adventure. With this change, the Company eliminated any further operational risk associated with the project while it continues its business relationship with Disney and maintains a presence at the theme park. As a result of this change, the Company has recorded special charges to date totaling \$12,240, or \$0.47 per diluted share, primarily reflecting fixed asset write-offs, employee separation expenses and lease cancellation fees. All exit costs accrued in prior periods associated with Disney's California Adventure were paid in full as of March 31, 2002.

During the first quarter of fiscal 2002, the Company also revised its volume growth expectations for the fiscal year to reflect the continued economic slowdown and a significant decrease in on-premise (i.e., hotel and restaurant) sales. As a result of these lowered volume growth expectations, the Company recorded \$3,750, or \$0.14 per diluted share, in inventory and fixed asset write-downs during the first quarter that were classified as cost of goods sold.

#### NOTE 5 COMPREHENSIVE INCOME

Comprehensive income includes revenues, expenses, gains and losses that are excluded from net income, including foreign currency translation adjustments and unrealized gains and losses on certain derivative financial instruments designated as cash-flow hedges. Comprehensive income for the three and nine months ended March 31, 2002 and 2001 were as follows:

	Unaudited		
	Three Months Ended March 31, 2002	2001	Nine 2002
	----	----	----
Net income	\$ 7,583	\$ 8,891	\$ 15,35

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Foreign currency translation adjustment, net of tax	(281)	173	(60)
Forward contracts, net of tax	37	- -	(2)
	-----	-----	-----
Comprehensive income	\$ 7,339	\$ 9,064	\$ 14,73
	=====	=====	=====

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

#### INTRODUCTION

During the first six months of fiscal 2002, the Company recorded \$12.2 million, or \$0.47 per diluted share, in special charges related to operational changes in its Disney California Adventure project. During the first quarter of fiscal 2002, the Company also recorded inventory and fixed asset write-downs, totaling \$3.8 million, or \$0.14 per diluted share, as a result of lowering its sales volume growth projections for the fiscal year. The adjusted figures discussed throughout this report, exclude the special charges and asset write-downs, as well as inventory step-up charges associated with business acquisitions for all periods presented.

The Company has included these adjusted figures in its discussion and analysis of financial condition and results of operations to provide better visibility into the results of its ongoing operations. The adjusted figures should not be considered an alternative to financial statements required under generally accepted accounting principles.

Effective July 1, 2001, the Company implemented new pronouncements issued by the Financial Accounting Standards Board's Emerging Issues Task Force that require certain sales incentives and fees paid to retailers to be recorded as reductions of revenue. The Company previously reported these expenses as selling, general and administrative expenses. Prior period financial statements have been restated to reflect this change in classification.

#### CRITICAL ACCOUNTING POLICIES

The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and the related disclosures of contingent assets and liabilities. Actual results could differ from those estimates under different assumptions or conditions. The Company believes that the following critical accounting policies affect its more significant estimates and judgements used in the preparation of its consolidated financial statements:

The Company determines its allowance for doubtful accounts based on the aging of accounts receivable balances, its historic write-off experience and the financial condition of its customers. Changes in the financial condition of the Company's major customers could result in significant accounts receivable write-offs.

The Company writes down its inventory for estimated obsolescence equal to the difference between the cost of the inventory and its estimated market value, which is based on historic experience and assumptions about market conditions and expected future demand. If actual market conditions and future demand are less favorable than projected, additional write-downs may be required.

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The Company has goodwill and license fees related to business acquisitions. The Company reviews these assets for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. The assessment of impairment is based on the estimated undiscounted future cash flows from operating activities, which is compared to the carrying amount of the assets. Write-downs are recorded when the estimated undiscounted future cash flows are lower than the assets' carrying value.

The Company carries deductibles for workers' compensation, medical and general liability claims, up to a maximum amount per claim. The Company accrues the undiscounted estimated liability based on its historic claims experience, estimated future claims costs and other factors.

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The Company is subject to litigation and other contingencies in the ordinary course of business. Liabilities related to commitments and contingencies are recognized when a loss is probable and reasonably estimable.

### RESULTS OF OPERATIONS

#### Third Quarter of Fiscal 2002 Compared to Third Quarter of Fiscal 2001

**Net Revenues** Net revenues decreased by 7.0%, reflecting a 1.0% increase in sales volume and a 7.9% decrease in net revenues per case. The decrease in net revenues per case was mainly due to a shift in sales mix from luxury wines to super premium wines, combined with an increase in certain promotional allowances, primarily for popular and super premium wines, that are now recorded as reductions of revenue.

**Cost of Goods Sold** Cost of goods sold as reported decreased by 4.3%. Adjusted cost of goods sold decreased by 4.8%, reflecting the shift in sales mix to super premium wines and lower grape costs overall.

**Gross Profit** As a result of the above factors, the reported gross profit percentage was 44.4% compared to 46.0% reported last year. The adjusted gross profit percentage decreased to 45.5% from 46.7% last year.

**Operating Expenses** Operating expenses decreased by 5.6%, reflecting the impact of cost cutting measures implemented during the fiscal year. However, the ratio of operating expenses to net revenues increased to 28.2% from 27.8% due to the loss of sales volume leverage.

**Interest** Interest expense decreased by 5.0%, reflecting decreases in the Company's average borrowings outstanding and average interest rate that were partially offset by a reduction of capitalized interest due to the completion of certain capital and vineyard development projects.

**Equity Income from Joint Ventures** Equity income from joint ventures as reported increased by \$0.9 million. Adjusted equity income from joint ventures, which excludes inventory step-up charges associated with the Ornellaia acquisition, increased by \$0.6 million. The increase in both the reported and adjusted figures was due mainly to improved profitability of the Chilean joint venture.

**Provision for Income Taxes** The Company's effective tax rate was 37.5% compared to 38.5% last year. The lower effective tax rate was primarily the result of an increase in certain deductible expenses and manufacturing tax credits.

**Net Income and Earnings Per Share** As a result of the above factors, net income as reported totaled \$7.6 million, or \$0.46 per diluted share, compared to \$8.9 million, or \$0.54 per diluted share, a year ago. Adjusted net income totaled



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\$8.7 million, or \$0.53 per diluted share, compared to \$10.0 million, or \$0.61 per diluted share, a year ago.

First Nine Months of Fiscal 2002 Compared to First Nine Months of Fiscal 2001

Net Revenues Sales volume decreased by 5.6% and net revenues decreased by 8.9%, reflecting the impact of the continued economic downturn combined with a sharp decline in the travel and entertainment sectors that began in September. Net revenues per case decreased by 3.5% to \$46.58 per case, reflecting a shift in sales mix from luxury wines to popular and super premium wines. Due to the continued economic slowdown and the decline in the travel and entertainment sectors, the Company expects sales volume, net revenues and net income to decrease compared to prior year levels for the fiscal year.

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Cost of Goods Sold Cost of goods sold as reported decreased by 7.8%. Adjusted cost of goods sold decreased by 9.7%, reflecting decreased sales volume, the shift in sales mix to popular and super premium wines and lower grape costs overall.

Gross Profit As a result of the above factors, the reported gross profit percentage was 43.6% compared to 44.3% reported last year. The adjusted gross profit percentage increased to 45.7% from 45.2% last year.

Operating Expenses Operating expenses as reported increased by 15.2% and the reported ratio of operating expenses to net revenues increased to 33.3% from 26.3% a year ago. Adjusted operating expenses increased by 1.8% and the adjusted ratio of operating expenses to net revenues increased to 29.4% from 26.3% a year ago. The increase in the adjusted operating expense ratio primarily reflects the loss of sales volume leverage.

Interest Interest expense increased by 6.6%, reflecting a reduction in capitalized interest due to the completion of certain capital and vineyard development projects that was partially offset by a decrease in the Company's average interest rate.

Equity Income from Joint Ventures Equity income from joint ventures as reported increased by \$1.6 million. Adjusted equity income from joint ventures, which excludes inventory step-up charges associated with the Ornellaia acquisition, increased by \$1.1 million. The increase in both the reported and adjusted figures was due mainly to improved profitability of the Chilean joint venture.

Provision for Income Taxes The Company's effective tax rate was 37.5% compared to 38.5% last year. The lower effective tax rate was primarily the result of an increase in certain deductible expenses and manufacturing tax credits.

Net Income and Earnings Per Share As a result of the above factors, net income as reported totaled \$15.4 million, or \$0.94 per diluted share, compared to \$32.9 million, or \$2.02 per diluted share, a year ago. Adjusted net income totaled \$28.5 million, or \$1.74 per diluted share, compared to \$36.6 million, or \$2.24 per diluted share, a year ago.

### LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents decreased by \$7.2 million during the first nine months of fiscal 2002 as cash used in operating and investing activities exceeded cash provided by financing activities. Cash used in operations totaled \$17.3 million, reflecting an increase in inventories that was partially offset by net income, as well as the non-cash impact on pre-tax income of depreciation and amortization, and a decrease in accounts receivable. The increase in inventories

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reflects a seasonal increase in inventories subsequent to harvest, as well as a build up of inventories resulting from grape commitments that were made prior to the Company lowering its sales forecast due to softening demand and a sharp decline in the travel and entertainment sectors. Cash used in investing activities totaled \$5.1 million, reflecting purchases of production equipment and vineyard development cost that were partially offset by proceeds from the sale of certain vineyard assets and distributions from joint ventures. Cash provided by financing activities totaled \$15.2 million, reflecting net additions of debt and a book overdraft of \$3.2 million, which represents the float on outstanding checks.

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The Company maintains master lease facilities that provide the capacity to fund up to \$189.0 million, of which \$142.8 million had been utilized as of March 31, 2002. The combined facilities enable the Company to lease certain real property and equipment to be constructed or acquired. The leases are classified as operating leases and they have initial terms of three to seven years, after a construction period, with options to renew. The Company may, at its option, purchase the property under lease during or at the end of the lease term. If the Company does not exercise the purchase option, the Company will guarantee a residual value of the property under lease, which was approximately \$118.5 million as of March 31, 2002.

The Company has unsecured long-term credit lines that have maximum credit availability of \$150.0 million and expire on December 14, 2004. The Company had \$83.0 million outstanding under its long-term credit lines as of March 31, 2002.

The Company also has the ability to borrow up to \$35.0 million under an uncommitted credit facility with a bank. The Company may request advances under this credit facility, and if approved by the bank, the advance must be repaid in no more than 180 days from the date of the advance. The Company had \$3.1 million outstanding under this credit facility as of March 31, 2002.

### PART II

Item 1. Legal Proceedings.

The Company is subject to litigation in the ordinary course of its business. In the opinion of management, the ultimate outcome of existing litigation will not have a material adverse effect on the Company's consolidated financial condition, the results of its operations or its cash flows.

Item 6. Exhibits and Reports on Form 8-K.

1) Exhibits:  
None

2) Form 8-K:  
No reports on Form 8-K were filed during the quarter ended March 31, 2002.

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### 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

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undersigned thereunto duly authorized.

THE ROBERT MONDAVI CORPORATION

Dated: May 15, 2002

By /s/ HENRY J. SALVO, JR.  
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Henry J. Salvo, Jr.

Chief Financial Officer

Forward-looking Statements

The above Form 10-Q and other information provided from time to time by the Company contain historical information as well as forward-looking statements about the Company, the premium wine industry and general business and economic conditions. Such forward-looking statements include, for example, projections or predictions about the Company's future growth, consumer demand for its wines, including new brands and brand extensions, margin trends, anticipated future investment in vineyards and other capital projects, the premium wine grape market and the premium wine industry generally. Actual results may differ materially from the Company's present expectations. Among other things, reduced consumer spending, a change in consumer preferences or the length and severity of the current economic downturn in some of the Company's key markets, including in particular the depressed travel and entertainment sectors, could reduce demand for the Company's wines. Similarly, competition from numerous domestic and foreign vintners, coupled with changes in foreign currency valuations, could affect the Company's volume and revenue growth outlook. The price of grapes, the Company's single largest product cost, is beyond the Company's control and higher grape costs may put more pressure on the Company's gross profit margin than is currently forecast. Interest rates and other business and economic conditions could change significantly the cost and risks of projected capital spending. For additional cautionary statements identifying important factors that could cause actual results to differ materially from such forward-looking information, please refer to Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations," in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2001, on file with the Securities and Exchange Commission. For these and other reasons, no forward-looking statement by the Company can nor should be taken as a guarantee of what will happen in the future.