ARTS WAY MANUFACTURING CO INC
Form 10-Q
July 15, 2003

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 Quarter Ended May 31, 2003 Commission File No. 0-5131

ART'S-WAY MANUFACTURING CO., INC.
(Exact name of registrant as specified in its charter)

DELAWARE	42-0920725
State of Incorporation	I.R.S. Employer Identification No.
Hwy 9 West, Armstrong, Iowa	50514
Address of principal executive offices	Zip Code

Registrant's telephone number, including area code: (712) 864-3131

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 __

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

Number of common shares outstanding as of March 21, 2003: 1,938,176

ART'S-WAY MANUFACTURING CO., INC.
CONDENSED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended		Year to Date	
	May 31, 2003	May 31, 2002	May 31, 2003	May 31, 2002
Net Sales	$ 2,432,516	$ 2,252,621	$ 4,941,393	$ 4,894,513
Cost of goods sold	1,634,639	1,611,101	3,505,088	3,682,393
Gross Profit	797,877	641,520	1,436,305	1,212,120
Operating Expenses:				
Engineering	15,256	15,758	34,179	30,637
Selling	152,041	130,539	280,235	251,436
General and administrative	327,402	398,738	679,829	807,363
Total expenses	494,699	545,035	994,243	1,089,436
Income from operations	303,178	96,485	442,062	122,684
Other expenses:				
Interest expense	30,994	34,225	48,973	94,814
Total other expenses	40,776	66,021	64,820	140,721
Income (loss) before income taxes	262,402	30,464	377,242	(18,037)
Income tax expense	-	-	2,031	-
Net income (loss)	$ 262,402	$ 30,464	$ 375,211	$ (18,037)

Net income (loss) per share:				
Basic	$ 0.14	$ 0.02	$ 0.19	$ (0.01)
Diluted	$ 0.13	$ 0.02	$ 0.19	$ (0.01)
Common shares and equivalent outstanding:				
Basic	1,938,176	1,938,176	1,938,176	1,677,956
Diluted	1,950,438	1,944,368	1,948,646	1,677,956

See accompanying notes to financial statements.

ART'S-WAY MANUFACTURING CO., INC.
CONDENSED BALANCE SHEETS
(Unaudited)

	May 31, 2003	November 30, 2002
ASSETS		
Current Assets		
Cash	$ 979,783	$ 75,358
Accounts receivable-customers, net of allowance for doubtful accounts of $59,000 and $50,000 in May and November, respectively	973,483	592,945
Other Receivables	110,000	-
Inventories	4,155,119	3,576,707
Other current assets	70,516	95,385
Total current assets	6,388,901	4,340,395
Property, plant and equipment, at cost	10,725,972	10,725,972
Less accumalated depreciation	9,891,000	9,751,260
Net property, plant and equipment	834,972	974,712
Inventories, noncurrent	430,509	430,509
Other assets	211,515	175,849
Total Assets	$ 7,865,897	$ 5,921,465
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Notes payable to bank	$ -	$ 319,222
Current portion of long-term debt	122,254	356,669
Accounts payable	252,352	523,492
Customer deposits	984,267	249,756
Accrued expenses	733,376	630,972
Total current liabilities	2,092,249	2,080,111
Long-term liabilities	159,777	187,204
Long-term debt, excluding current portion	2,105,340	520,830
Total liabilities	4,357,366	2,788,145
Stockholders' Equity		
Common stock - $.01 par value. Authorized 5,000,000 shares; issued 1,938,176 shares in May and in November	19,382	19,382
Additional paid-in capital	1,634,954	1,634,954
Retained earnings	1,854,195	1,478,984
Total stockholders' equity	3,508,531	3,133,320
Total liabilities and stockholders' equity	$ 7,865,897	$ 5,921,465

See accompanying notes to financial statements.

CONDENSED STATEMENTS OF CASH FLOWS
(Unaudited)

	Six Months Ended May 31, 2003	Six Months Ended May 31, 2002
CASH FLOW FROM OPERATIONS:		
Net income (loss)	$ 375,211	$ (18,037)
Adjustment to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	139,740	121,908
Changes in working capital components:		
(Increase) decrease in:		
Accounts receivable	(380,538)	102,324
Other receivables	(110,000)	-
Inventories	(578,412)	208,261
Other current assets	(75,131)	(246,972)
Other, Net	(35,666)	-
Increase (decrease) in:		
Accounts payable	(271,140)	(154,849)
Customer deposits	734,511	786,601
Accrued expenses	102,404	41,968
Net cash provided by (used in) operating activities	(99,021)	841,204
CASH FLOW FROM INVESTING ACTIVITIES:		
Purchases of property, plant and equipment	-	-
CASH FLOW FROM FINANCING ACTIVITIES:		
Proceeds from (payments of) notes payable to bank	1,322,668	(1,452,572)
Principal payments on term debt	(319,222)	(178,409)
Proceeds from issuance of common stock from treasury	-	53,253
Proceeds from issuance of common stock	-	746,747
Net cash provided by (used in) financing activities	1,003,446	(830,981)
Net increase in cash	904,425	10,223
Cash at beginning of period	75,358	4,375
Cash at end of period	$ 979,783	$ 14,598
Supplemental disclosures of cash flow information:		
Cash paid during the year for:		
Interest	$ 48,973	$ 94,814
Income taxes	3,301	4,032

See accompanying notes to financial statements.

ART'S-WAY MANUFACTURING CO., INC.
NOTES TO CONDENSED FINANCIAL STATEMENTS
(Unaudited)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Statement Presentation

The financial statements are unaudited and reflect all adjustments (consisting only of normal recurring adjustments) which are, in the opinion of management, necessary for a fair presentation of the financial position and operating results for the interim periods. The financial statements should be read in conjunction with the financial statements and notes thereto contained in the Company's Annual Report on Form 10-K for the year ended November 30, 2002. The results of operations for the second quarter and year to date ended May 31, 2003 are not necessarily indicative of the results for the fiscal year ending November 30, 2003.

2. INCOME (LOSS) PER SHARE

Basic net income (loss) per common share is computed on the basis of weighted average number of common shares outstanding. Diluted net income (loss) per share has been computed on the basis of weighted average number of common shares outstanding plus equivalent shares assuming exercise of stock options.

The difference in shares utilized in calculating basic and diluted net income (loss) per share represents the number of shares issued under the Company's stock option plans less shares assumed to be purchased with proceeds from the exercise of the stock options. The reconciling item between the shares used in the computation of basic and diluted earnings per share is 12,262 for the second quarter ended May 31, 2003; 6,192 for the second quarter ended May 31, 2002; and 10,470 for the year to date period ended May 31, 2003 equivalent shares for the effect of dilutive stock options. Due to the net loss for the year to date period ended May 31, 2002, the anti-dilutive effect of the Company's stock option plans is not included in the calculation of diluted loss per share for that period.

3. INVENTORIES

Major classes of inventory are:	May 31,2003	November 30, 2002
Raw material	$ 931,564	$ 1,065,166
Work-in-process	1,653,737	1,209,007
Finished goods	2,000,327	1,733,043
Total	$ 4,585,628	$ 4,007,216
Less inventories classified as noncurrent	430,509	430,509
Inventories, current	$ 4,155,119	$ 3,576,707

4. ACCRUED EXPENSES

Major components of accrued expenses are:	May 31,2003	November 30, 2002
Salaries, wages and commissions	$ 356,244	$ 294,220
Accrued warranty expense	59,495	60,232
Other	317,637	276,520
Total	$ 733,376	$ 630,972

5. LOAN AND CREDIT AGREEMENTS

On April 25, 2003 the Company obtained long-term financing through West Des Moines State Bank (West Bank), West Des Moines, Iowa. Credit facilities consist of two loan agreements totaling $5,500,000.

Facility #1 is a revolving line of credit for $2,500,000 with advances funding the working capital, letter of credit and corporate credit card needs. It renews annually with a maturity date of February 28, 2004. The interest rate will be West Bank's prime interest rate plus 1% adjusted daily. Monthly interest only payments will be required and the unpaid principal due on the maturity date. In addition an annual fee of $12,500 will be paid for the use of this credit facility. Collateral consists of a first position on assets owned by the Company including, but not limited to inventories, accounts receivable, machinery and equipment.

Facility #2 is long-term financing for up to $3,000,000 that is supported by a guarantee issued by the United States Department of Agriculture (USDA) for 75% of the loan amount outstanding. The loan refinanced existing debt to UPS Capital (approximately $1,500,000), finance equipment (approximately $250,000), provide permanent working capital (approximately $500,000) and satisfy closing costs (approximately $50,000). Approximately $700,000 will be reserved for future acquisitions. Maturity date is March 31, 2023. The variable interest rate will be West Bank's prime interest rate plus 1.5% adjusted daily. Monthly principal and interest payments will be amortized over 20 years, at which time the loan will mature. A one-time origination fee of 1% was also required. Collateral for Facility #2 is primarily real estate with a second position on assets of Facility #1. The USDA subordinates collateral rights in all assets other than real estate in an amount equal to West Bank's other credit commitments.

J. Ward McConnell, Jr. was required to personally guarantee Facility #1 and Facility #2 on an unlimited and unconditional basis. The guarantee of Facility #2 shall then be reduced after the first three years to a percentage representing his ownership of the Company. Mr. McConnell's guarantee shall be removed from Facility #2 in the event that his ownership interest in the Company is reduced to a level less than 20% after the first three years of the loan. The Company will compensate Mr. McConnell for his personal guarantee at an annual percentage rate of 2% of the outstanding balance to be paid monthly.

Other terms and conditions are providing monthly internally prepared financial reports including accounts receivable aging schedules and borrowing base certificates and year-end audited financial statements. The borrowing bases shall limit advances from Facility #1 to 60% of accounts receivable less than 90 days, 60% of finished goods inventory, 50% of raw material inventory and 50% of work-in-process inventory plus 40% of appraisal value of machinery and equipment. Covenants include debt service coverage ratio, debt/tangible net worth ratio, current ratio, limit capital expenditures, and maintain a minimum tangible net worth.

On April 25, 2003 the Company borrowed $2,000,000 against Facility #2. $1,528,775 was used to payoff UPS Capital with $110,000 being held in reserve for a letter of credit ($100,000) and any additional fees. The balance of $471,225 was used as working capital. As of May 31, 2003, the Company has not borrowed against Facility #1.

A summary of the Company's term debt is as follows:

	May 31, 2003	November 30, 2002
West Bank real estate loan payable in monthly Installments of $17,776 including interest at Bank's prime rate plus 1.5% (5.75%)	$ 1,991,807	$ -
Installment term debt payable in monthly Installments of $23,700, plus interest at four percent over the bank's national money market rate due on demand, secured	$ -	$ 605,371
State of Iowa Community Development		

Block Grant promissory notes at zero percent interest, maturity 2006, with quarterly principal payments of $11,111	$ 144,444	$ 166,667
State of Iowa Community Development Block Grant local participation promissory notes at 4% interest, Maturity 2006, with quarterly payments of $7,007	$ 91,343	$ 105,461
Total term debt	$ 2,227,594	$ 877,499
Less current portion of term debt	$ 122,254	$ 356,669
Term debt, excluding current portion	$ 2,105,340	$ 520,830

6. RELATED PARTY TRANSACTION

In February 2002, the Company sold common stock to an existing shareholder, Mr. J. Ward McConnell, Jr., at estimated fair value. Proceeds from the sale of the stock were $800,000. Mr. McConnell has agreed that without prior approval of the Board of Directors, excluding himself and his son, he will not acquire as much as fifty percent (50%) of the Company's common stock and will not take the Company private. Immediately after the transaction, Mr. McConnell was elected as Chairman of the Board of Directors of the Company. His son, Marc McConnell, is also a Board Member.

Item 2

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

(a) Liquidity and Capital Resources

The Company's main source of funds for the six months ended May 31, 2003 came by securing long-term financing (see footnote 5 of the notes to the condensed financial statements) and from receiving advance payments from customers on sugar beet equipment to be delivered in the third quarter.

These sources were offset by increases of the accounts receivable, other receivables and inventories. The increase in accounts receivable results from the sales of sugar beet equipment and parts stock orders in May 2003. Other receivables of $110,000 is monies held in reserve for a letter of credit that expired May 31, 2003 and additional fees associated with the UPS Capital payoff. Current production of sugar beet harvesters, the biggest single piece of equipment produced, and finished goods in stock, mainly grinder/mixers, defoliators and graders, are the reason for inventories increase.
Other offsets include the reduction of accounts payable.

The net cash from financing activities of $1,003,446 combined with the negative cash flow from operation of $99,021 had a net increase in cash of $904,425 for the six months ended May 31, 2003. The Company had no material commitments for capital expenditures.

On July 14, 2003 Art's-Way announced that it entered into an agreement to purchase OBECO Incorporated, a manufacturer of steel truck bodies located in Cherokee, Iowa. The agreement includes the purchase of real estate, all inventory, intellectual materials, machinery, tooling, fixtures and the company name. The name of the Company will change to Cherokee Truck Bodies, Incorporated, but the truck bodies will continue to be sold under the recognized name OBECO. The company will continue to be located in Cherokee, Iowa.

The United States Bankruptcy Court has approved the sale and the anticipated closing date for the acquisition is set for July 25, 2003. It is anticipated that this transaction will cost approximately $500,000.

This acquisition fits in with Art's-Way metal fabrication capability and provides diversification to its agricultural implement product offerings. We believe this action will facilitate growing the business and improving shareholder value.

(b) Results of Operations

Fiscal year 2003 second quarter and year to date net sales were 8% and 1%, respectively, higher than for the comparable periods one-year ago. The sales mix of Art's-Way products and OEM products shifted. OEM sales increased and Art's-Way brand sales decreased by 15% when comparing second quarter 2003 to 2002 and 11% for the year to date 2003 and 2002.

Gross profit, as a percent of sales, was 33% for the quarter ended May 31, 2003, as compared to 28% for the same period in 2002. Year to date through May 31, 2003, gross profit was 29% compared to 25% for the prior year. The increase of labor efficiency by 15 points and continued cost reduction programs has resulted in this increase.

Operating expenses were lower than last year. As a percent of sales, operating expenses were 20% and 24% for the three months ended May 31, 2003 and 2002, respectively. Year to date ended May 31, 2003 and 2002, operating expenses were 20% and 22%, respectively. Selling expenses increased by $21,502 for the quarter and $28,799 year to date compared to the same periods of the previous year. The Company has increased exposure of Art's-Way products both regionally and nationally through advertisement, direct mailing and trade shows. General and administrative expenses decreased $71,336 for the quarter and $127,534 year to date compared to the same periods of the previous year. The decrease is primarily due to changing the health insurance plan offered to the employees.

Other expenses decreased by $25,245 for the quarter and $75,901 year to date from the previous year. Reduction in bank borrowings combined with lower interest rates and reduced volume in our financed accounts receivable resulted in this reduction.

The order backlog as of May 31, 2003 is $2,798,000, compared to $2,994,000 one year ago. These orders primarily will be delivered in the third quarter of the current fiscal year. The current year backlog includes $1,232,000 in orders for beet equipment compared to $1,376,000 last year at this time. Potato harvester is $329,000 and OEM backlog is $284,000 to be shipped in the third quarter.

(c) Critical Accounting Policies

The Company's critical accounting policies involving the more significant judgments and assumptions used in the preparation of the financial statements as of May 31, 2003 have remained unchanged from November 30, 2002. These policies involve revenue recognition, inventory valuation and income taxes. Disclosure of these critical accounting policies is incorporated by reference under Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operation" in the Company's Annual report on Form 10-K for the year ended November 30, 2002.

Item 3

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS

The Company does not have any additional market risk exposure other than what was outlined in the November 30, 2002, 10-K filing.

Item 4
DISCLOSURE CONTROLS AND PROCEDURES

Within 90 days of the filing date of this quarterly report, the Company's Chief Executive Officer and Finance Manager have evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Exchange Act Rules 13a-14(c) and 15(d)-14(c)) and, based on their evaluation, have concluded that the disclosure controls and procedures are effective. There were no significant changes in the Company's internal controls or in other factors that could significantly affect these controls subsequent to the date of their evaluation, including any corrective action with regard to significant deficiencies and material weaknesses.

Part II - Other Information

ITEM 1. LITIGATION AND CONTINGENCIES

Various legal actions and claims are pending against the Company. In the opinion of management, adequate provisions have been made in the accompanying financial statements for all pending legal actions and other claims.

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

On April 24, 2003, the Company held an annual meeting of shareholders for the purpose of: (1) to elect seven (7) directors to serve until the next annual meeting of shareholders or until such time as their successors are elected and qualified; 2) to consider and vote upon a proposal to approve the 2001 Director Stock Option Plan; and 3) to consider and vote upon a proposal to ratify the appointment of McGladrey & Pullen, LLP as independent public accountants of the Company for the year ending November 30, 2003.

The following information is submitted:

(a) An annual meeting was held on April 24, 2003.

(b) The following directors were all of the nominees and were elected by the shareholders:

David R. Castle	George A. Cavanaugh, Jr.
James L. Koley	Douglas McClellan
J. Ward McConnell, Jr.	Marc H. McConnell
Thomas E. Buffamante	

(c) The shareholders voted on a motion to approve the 2001 Directors Stock Option Plan.
Total number of shares authorized to vote: 1,938,176
Total number of shares voted in favor: 1,625,872
Total number of shares voted against: 33,906
Total number of abstentions: 14,721

(d) The shareholders voted on a motion to ratify the selection of McGladrey & Pullen, LLP as independent public accountants for the year ending November 30, 2003.
Total number of shares authorized to vote: 1,938,176
Total number of shares voted in favor: 1,668,350
Total number of shares voted against: 5,849
Total number of abstentions: 300

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits:

10.7 Long-term financing agreements, mortgage note and guarantee for both loans with West Bank
99.1 Certification of Financial Statements

(b) Reports on Form 8-K:
Long-term financing filed 5/2/03

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.

ART'S-WAY MANUFACTURING CO., INC.

Date: April 14, 2003 By: /s/ John C. Breitung

John C. Breitung
President and Chief Executive Officer

Date: April 14, 2003 By: /s/ Seth F. LaBore

Seth F. LaBore
Finance Manager

CERTIFICATIONS

I, John C. Breitung, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Art's-Way Manufacturing Co., Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: July 14, 2003

/s/ John C. Breitung

President and Chief Executive Officer

OM504759.1

CERTIFICATIONS

I, Seth F. LaBore, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Art's-Way Manufacturing Co., Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: July 14, 2003

/s/ Seth F. LaBore
Finance Manager

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