

Edgar Filing: ESCALADE INC - Form 10-Q

ESCALADE INC
Form 10-Q
October 27, 2006

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 October 7, 2006

Commission File Number 0-6966

ESCALADE, INCORPORATED

(Exact name of registrant as specified in its charter)

| | |
|--------------------------|--------------|
| Indiana | 13-2739290 |
| ----- | ----- |
| (State of incorporation) | (I.R.S. EIN) |

817 Maxwell Avenue, Evansville, Indiana 47711

(Address of principal executive office)

812-467-1334

(Registrant's Telephone Number)

Securities registered pursuant to Section 12(b) of the Act
NONE

Securities registered pursuant to section 12(g) of the Act

Common Stock, No Par Value

(Title of Class)

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 No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer

Indicate by checkmark whether the registrant is a shell company (as defined in

Edgar Filing: ESCALADE INC - Form 10-Q

Rule 12 b-2 of the Exchange Act).

Yes [] No [X]

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 October 24 ,2006 |
|----------------------|---------------------------------|
| Common, no par value | 13,026,275 |

INDEX

| | Page No. |
|--|-------------|
| Part I. Financial Information: | |
| Item 1 - Financial Statements: | |
| Consolidated Condensed Balance Sheets as of October 7, 2006 (Unaudited), October 1, 2005 (Unaudited), and December 31, 2005 | 3 |
| Consolidated Condensed Statements of Income (Unaudited) for the Three Months and Nine Months Ended October 7, 2006 and October 1, 2005 | 4 |
| Consolidated Condensed Statements of Comprehensive Income (Unaudited) for the Three Months and Nine Months Ended October 7, 2006 and October 1, 2005 | 4 |
| Consolidated Condensed Statements of Cash Flows (Unaudited) for the Nine Months Ended October 7, 2006 and October 1, 2005 | 5 |
| Notes to Consolidated Condensed Financial Statements (Unaudited) | 6 |
| Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operations | 11 |
| Item 3 - Quantitative and Qualitative Disclosures about Market Risk | 13 |
| Item 4 - Controls and Procedures | 14 |
| Part II. Other Information | |
| Item 2 - Issuer Purchases of Equity Securities | 15 |
| Item 6 - Exhibits | 16 |
| Signatures | 16 |

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Edgar Filing: ESCALADE INC - Form 10-Q

ESCALADE, INCORPORATED AND SUBSIDIARIES
CONSOLIDATED CONDENSED BALANCE SHEETS
(All amounts in thousands except share information)

| | October 7, 2006 | October 1, 2005 | December 31, 2005 |
|---|----------------------|----------------------|----------------------|
| | ----- (Unaudited) | ----- (Unaudited) | ----- (Audited) |
| ASSETS | | | |
| Current Assets: | | | |
| Cash and cash equivalents | \$ 339 | \$ 3,028 | \$ 3,017 |
| Receivables, less allowance of \$2,391; \$2,449; and \$1,544; respectively | 49,517 | 50,682 | 31,744 |
| Inventories | 40,426 | 37,443 | 33,049 |
| Prepaid expenses | 2,409 | 1,479 | 1,559 |
| Deferred income tax benefit | 1,723 | 1,923 | 1,818 |
| | ----- | ----- | ----- |
| TOTAL CURRENT ASSETS | 94,414 | 94,555 | 71,187 |
| Property, plant and equipment, net | 20,290 | 18,245 | 20,307 |
| Intangible assets | 20,895 | 6,866 | 6,634 |
| Goodwill | 24,708 | 17,234 | 17,157 |
| Investments | 7,790 | 6,120 | 7,786 |
| Interest rate swap | 273 | 60 | 181 |
| Other assets | 2,029 | 2,432 | 2,044 |
| | ----- | ----- | ----- |
| | \$ 170,399 | \$ 145,512 | \$ 125,296 |
| | ===== | ===== | ===== |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | | |
| Current liabilities: | | | |
| Notes payable | \$ 24,534 | \$ 10,590 | \$ -- |
| Current portion of long-term debt | -- | 1,066 | -- |
| Trade accounts payable | 10,071 | 10,835 | 3,518 |
| Accrued liabilities | 25,640 | 24,245 | 24,429 |
| Income tax payable | 1,598 | 517 | 1,854 |
| | ----- | ----- | ----- |
| TOTAL CURRENT LIABILITIES | 61,843 | 46,187 | 30,867 |
| Other Liabilities: | | | |
| Long-term debt | 28,020 | 25,338 | 18,487 |
| Deferred compensation | 1,025 | 1,320 | 1,349 |
| | ----- | ----- | ----- |
| | 90,888 | 72,845 | 50,703 |
| Stockholders' equity: | | | |
| Preferred stock: | | | |
| Authorized 1,000,000 shares; no par value, none issued | | | |
| Common stock: | | | |
| Authorized 30,000,000 shares; no par value, issued and outstanding - 13,029,769; 13,010,733; and 12,946,869; respectively | 13,030 | 13,011 | 12,947 |
| Retained earnings | 63,984 | 58,327 | 60,696 |
| Accumulated other comprehensive income | 2,497 | 1,329 | 950 |
| | ----- | ----- | ----- |
| | 79,511 | 72,667 | 74,593 |
| | ----- | ----- | ----- |

Edgar Filing: ESCALADE INC - Form 10-Q

\$ 170,399 \$ 145,512 \$ 125,296
 =====

See notes to Consolidated Condensed Financial Statements.

3

ESCALADE, INCORPORATED AND SUBSIDIARIES
 CONSOLIDATED CONDENSED STATEMENTS OF INCOME (UNAUDITED)
 (All amounts in thousands, except per share amounts)

| | Three Months Ended | | Ni |
|--|--------------------|--------------------|-------|
| | October 7, 2006 | October 1, 2005 | |
| Net sales | \$ 65,583 | \$ 63,557 | \$ 14 |
| Costs, expenses and other income: | | | |
| Cost of products sold | 49,023 | 46,148 | 10 |
| Selling, general and administrative expenses | 10,650 | 8,935 | 3 |
| Operating income | 5,910 | 8,474 | 1 |
| Interest expense, net | (862) | (345) | (|
| Other income (expense) | (310) | 225 | |
| Income before income taxes | 4,738 | 8,354 | |
| Provision for income taxes | 1,746 | 2,902 | |
| Net income | \$ 2,992 | \$ 5,452 | \$ |
| Per Share Data: | | | |
| Basic earnings per share | \$ 0.23 | \$ 0.42 | \$ |
| Diluted earnings per share | \$ 0.23 | \$ 0.41 | \$ |
| Cash dividend paid | -- | -- | \$ |

CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

| | | | |
|---|----------|----------|----|
| Net income | \$ 2,992 | \$ 5,452 | \$ |
| Unrealized gain (loss) on securities, net of tax of \$(111), \$20, \$(36) and \$18, respectively | 168 | (31) | |
| Foreign currency translation adjustment, net of tax of \$(261), \$(20), \$(945) and \$2,301, respectively | 395 | 30 | |
| Unrealized gain on interest rate swap agreement, net of tax of \$21, \$(65), \$(40) and \$(191), respectively | (32) | 99 | |

Edgar Filing: ESCALADE INC - Form 10-Q

| | | | |
|----------------------|----------|----------|----|
| Comprehensive income | \$ 3,523 | \$ 5,550 | \$ |
|----------------------|----------|----------|----|

See notes to Consolidated Condensed Financial Statements.

4

ESCALADE, INCORPORATED AND SUBSIDIARIES
CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS (UNAUDITED)
(All amounts in thousands)

| | Nine Months Ended | |
|--|--------------------|--------------------|
| | October 7, 2006 | October 1, 2005 |
| Operating Activities: | | |
| Net income | \$ 5,388 | \$ 8,861 |
| Depreciation and amortization | 4,553 | 3,651 |
| Adjustments necessary to reconcile net income to net cash provided by operating activities | (12,567) | (9,774) |
| Net cash provided (used) by operating activities | (2,626) | 2,738 |
| Investing Activities: | | |
| Purchase of property and equipment | (1,903) | (5,166) |
| Proceeds from asset disposition | -- | 68 |
| Acquisition of assets | (28,619) | (3,213) |
| Net cash used by investing activities | (30,522) | (8,311) |
| Financing Activities: | | |
| Net increase in notes payable | 32,898 | 8,780 |
| Proceeds from exercise of stock options | 1,288 | 308 |
| Director fees paid by issuing stock | 141 | 95 |
| Purchase of common stock | (1,376) | (1,391) |
| Dividends paid | (2,604) | (1,961) |
| Net cash provided by financing activities | 30,347 | 5,831 |
| Effect of exchange rate changes on cash | 123 | (280) |
| Net decrease in cash and cash equivalents | (2,678) | (22) |
| Cash and cash equivalents, beginning of period | 3,017 | 3,050 |
| Cash and cash equivalents, end of period | \$ 339 | \$ 3,028 |

See notes to Consolidated Condensed Financial Statements.

5

ESCALADE, INCORPORATED AND SUBSIDIARIES

Edgar Filing: ESCALADE INC - Form 10-Q

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (UNAUDITED)

Note A - Basis of Presentation

The significant accounting policies followed by the Company and its wholly owned subsidiaries for interim financial reporting are consistent with the accounting policies followed for annual financial reporting. All adjustments that are of a normal recurring nature and are in the opinion of management necessary for a fair statement of the results for the periods reported have been included in the accompanying consolidated condensed financial statements. The condensed consolidated balance sheet of the Company as of December 31, 2005 has been derived from the audited consolidated balance sheet of the Company as of that date. Certain information and note disclosures normally included in the Company's annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Form 10-K annual report for 2005 filed with the Securities and Exchange Commission.

Note B - Seasonal Aspects

The results of operations for the three month and nine month periods ended October 7, 2006 and October 1, 2005 are not necessarily indicative of the results to be expected for the full year.

Note C - Inventories

| (All amounts in thousands) | October 7, 2006 | October 1, 2005 | December 31, 2005 |
|----------------------------|--------------------|--------------------|----------------------|
| Raw materials | \$ 9,173 | \$ 7,076 | \$ 7,128 |
| Work in progress | 7,008 | 8,090 | 5,358 |
| Finished goods | 24,245 | 22,277 | 20,563 |
| | ----- | ----- | ----- |
| | \$ 40,426 | \$ 37,443 | \$ 33,049 |
| | ===== | ===== | ===== |

Note D - Notes Payable

On June 30, 2006, the Company executed a seventh amendment to the revolving term agreement that effectively increased the current available borrowing limit under the Euro Revolving Loan from Euro 2.5 million (\$3.2 million) to Euro 3.0 million (\$3.8 million) and extended the due date to May 19, 2008. All other terms of the agreement were unchanged. As of October 7, 2006 the outstanding balance on this line was Euro 1.5 million (\$1.9 million).

On June 30, 2006, the Company's wholly owned subsidiary, Indian-Martin, Inc., executed a second amendment to its revolving term agreement that extended the maturity due date to June 30, 2008. All other terms of the agreement were unchanged. As of October 7, 2006 the outstanding balance on this line was \$24.5 million.

On June 1, 2006, the Company executed a sixth amendment to the revolving term

Edgar Filing: ESCALADE INC - Form 10-Q

agreement that maintained the current available borrowing limit at \$31 million and delayed the annual reduction of \$7 million until May 19, 2007. All other terms of the agreement were unchanged. As of October 7, 2006 the outstanding balance on this line was \$23.4 million.

Note E - Income Taxes

The provision for income taxes was computed based on financial statement income.

6

Note F - Employee Stock Option Plan

The Company has two stock-based compensation plans. Prior to the start of the current fiscal year, the Company accounted for these plans under the recognition and measurement principles of APB Opinion No. 25, Accounting for Stock issued to Employees, and related interpretations. Beginning with the current fiscal year, the Company expenses the fair value of options to employee compensation expense in accordance with SFAS 123R Share-Based Payment (SFAS 123R). During the three months and nine months ended October 7, 2006, the Company recorded compensation expense of \$298 thousand and \$726 thousand, respectively.

The following table illustrates the effect on net income and earnings per share had the Company applied the fair value provisions of FASB Statement No. 123, Accounting for Stock-Based Compensation, to stock-based employee compensation for the three months and nine months ended October 1, 2005.

| (In Thousands Except Per Share Amounts) | Three months ended October 1, 2005 |
|---|---------------------------------------|
| Net income, as reported | \$ 5,452 |
| Less: Total stock-based employee compensation cost determined under the fair value based method, net of income taxes | (279) |
| Pro forma net income | \$ 5,173 |
| Earnings per share | |
| Basic--as reported | \$ 0.42 |
| Basic--pro forma | \$ 0.40 |
| Diluted--as reported | \$ 0.41 |
| Diluted--pro forma | \$ 0.39 |

Note G - Segment Information

Edgar Filing: ESCALADE INC - Form 10-Q

For the Three Months
Ended October 7, 2006

| In thousands | Sporting Goods | Office Products | Corp. |
|----------------------------------|-------------------|--------------------|-------|
| Revenues from external customers | \$ 51,967 | \$ 13,616 | \$ -- |
| Operating income (loss) | 5,094 | 1,800 | (984) |
| Net income | 2,051 | 854 | 87 |

As of and for the Nine Months
Ended October 7, 2006

| In thousands | Sporting Goods | Office Products | Corp. |
|----------------------------------|-------------------|--------------------|-----------|
| Revenues from external customers | \$ 105,027 | \$ 42,305 | \$ -- |
| Operating income (loss) | 8,017 | 6,334 | (3,136) |
| Net income (loss) | 2,964 | 3,425 | (1,001) |
| Total assets | \$ 112,815 | \$ 46,534 | \$ 11,050 |

7

For the Three Months
Ended October 1, 2005

| In thousands | Sporting Goods | Office Products | Corp. |
|----------------------------------|-------------------|--------------------|-------|
| Revenues from external customers | \$ 49,736 | \$ 13,821 | \$ -- |
| Operating income (loss) | 7,114 | 1,528 | (168) |
| Net income | 4,249 | 786 | 417 |

As of and for the Nine Months
Ended October 1, 2005

| In thousands | Sporting Goods | Office Products | Corp. |
|----------------------------------|-------------------|--------------------|-----------|
| Revenues from external customers | \$ 92,326 | \$ 48,564 | \$ -- |
| Operating income (loss) | 10,117 | 5,617 | (1,612) |
| Net income (loss) | 5,747 | 3,325 | (211) |
| Total assets | \$ 88,702 | \$ 44,489 | \$ 12,321 |

Note H - Dividend Payment

On March 24, 2006, the Company paid a dividend of \$0.20 per common share to all

Edgar Filing: ESCALADE INC - Form 10-Q

shareholders of record on March 17, 2006. The total amount of the dividend was \$2.6 million and was charged against retained earnings.

Note I - Earnings Per Share

The shares used in computation of the Company's basic and diluted earnings per common share are as follows:

| | Three Months October 7, 2006 |
|--|---------------------------------|
| All amounts in thousands | |
| Weighted average common shares outstanding | 13,026 |
| Dilutive effect of stock options | 30 |
| | 13,056 |
| | 13,056 |
| | |
| | Nine Months October 7, 2006 |
| All amounts in thousands | |
| Weighted average common shares outstanding | 13,007 |
| Dilutive effect of stock options | 33 |
| | 13,040 |
| | 13,040 |

Stock options that are anti-dilutive as to earnings per share are ignored in the computation of dilutive earnings per share. The number of employee stock options that were anti-dilutive in 2006 and 2005 was 613,800 and 167,800, respectively.

Note J - Acquisitions

In February 2006, the Company purchased substantially all of the assets of Family Industries, Inc., which manufactures and sells premium quality residential playground systems made from stained redwood under the WoodPlay brand. Combined with the acquisition of the ChildLife product line in the first quarter of fiscal 2005, this acquisition greatly enhances the breadth of the product offering and expands the Company's potential customer base. Playground systems will continue to be sold under both the Woodplay and ChildLife brand names, primarily through specialty dealers. The operating results from this acquisition have been included in the Sporting Goods business segment results

since the date of acquisition. The total price paid, which was paid in cash using the Company's revolving credit lines, exceeded the estimated fair market value of the net assets acquired resulting in \$4.8 million in Goodwill. The Goodwill recorded will be deductible for income tax purposes. The estimated fair

Edgar Filing: ESCALADE INC - Form 10-Q

market value of the assets acquired and liabilities assumed as of the date of acquisition are as follows:

| (All amounts in thousands) | Amount |
|-----------------------------|----------|
| | ----- |
| Current assets | \$ 2,865 |
| Property, plant & equipment | 50 |
| Other assets | 112 |
| Goodwill | 4,767 |
| | ----- |
| Total assets acquired | 7,794 |
| | |
| Current liabilities | (654) |
| | ----- |
| Net assets acquired | \$ 7,140 |
| | ===== |

In April 2006, the Company acquired all of the outstanding stock of Desmar Seguridad Y Archivo, S.L. ("Desmar"), a distributor of office products located in Barcelona, Spain. The Company acquired Desmar to solidify its presence in Spain. The operating results from this acquisition have been included in the Office Products business segment results since the acquisition date and the Company intends to operate this acquisition as a wholly owned distributor from its existing location. The total purchase price of EUR 1.9 million (\$2.4 million) was paid in cash and financed through the Company's current Euro debt facilities. The purchase price exceeded the estimated fair market value of the assets acquired resulting in Goodwill of \$2.2 million. The Goodwill recorded will not be deductible for income tax purposes. The estimated fair market value of the assets acquired and liabilities assumed as the date of acquisition are as follows:

| (All amounts in thousands) | Amount |
|-----------------------------|----------|
| | ----- |
| Current assets | \$ 1,383 |
| Property, plant & equipment | 177 |
| Other assets | 493 |
| Goodwill | 2,238 |
| | ----- |
| Total assets acquired | 4,291 |
| | |
| Current liabilities | (1,913) |
| | ----- |
| Net assets acquired | \$ 2,378 |
| | ===== |

In May 2006, the Company acquired substantially all of the assets of Carolina Archery Products which manufactures and distributes archery accessories. This acquisition expands the Company's product offerings in archery accessories and provides the Company with valuable technology rights that will be used to enhance its competitive position in the market place. The operating results from this acquisition have been included in the Sporting Goods business segment results since the date of acquisition. The total purchase price of \$18.9 million was paid in cash and financed through the Company's current debt facilities. The estimated fair market value of the assets acquired and liabilities assumed as the date of acquisition are as follows:

| (All amounts in thousands) | Amount |
|-----------------------------|----------|
| | ----- |
| Current assets | \$ 3,358 |
| Property, plant & equipment | 67 |
| Patent & other intangibles | 15,447 |
| | ----- |

Edgar Filing: ESCALADE INC - Form 10-Q

Net assets acquired \$ 18,872
=====

9

The following table presents unaudited pro forma financial information as if the Carolina Archery acquisition described above had occurred at the beginning of the respective periods:

| (In Thousands Except Per Share Amounts) | Three months ended | |
|---|--------------------|-----------------|
| | October 7, 2006 | October 1, 2005 |
| Net revenue: | | |
| Net revenue excluding Carolina Archery Products acquisition | \$ 61,718 | \$ 63,557 |
| Net revenue of Carolina Archery Products | 3,865 | 3,500 |
| Consolidation adjustment | -- | -- |
| Pro forma net revenues | \$ 65,583 | \$ 67,057 |
| Net income: | | |
| Net income excluding Carolina Archery Products acquisition | \$ 2,795 | \$ 5,452 |
| Net income of Carolina Archery Products | 543 | 1,216 |
| Consolidation adjustment | (346) | (490) |
| Pro forma net income | \$ 2,992 | \$ 6,178 |
| Basic earning per share: | | |
| Excluding Carolina Archery Products acquisition | \$ 0.21 | \$ 0.42 |
| Carolina Archery Products | 0.04 | 0.09 |
| Consolidation adjustment | (0.02) | (0.04) |
| Pro forma basic earnings per share | \$ 0.23 | \$ 0.47 |

| (In Thousands Except Per Share Amounts) | Nine months ended | |
|---|-------------------|-----------------|
| | October 7, 2006 | October 1, 2005 |
| Net revenue: | | |
| Net revenue excluding Carolina Archery Products acquisition | \$ 140,800 | \$ 140,890 |
| Net revenue of Carolina Archery Products | 8,984 | 7,700 |
| Consolidation adjustment | -- | -- |
| Pro forma net revenues | \$ 149,784 | \$ 148,590 |
| Net income: | | |
| Net income excluding Carolina | | |

Edgar Filing: ESCALADE INC - Form 10-Q

| | | | | |
|---|----|--------|----|---------|
| Archery Products acquisition | \$ | 4,881 | \$ | 8,861 |
| Net income of Carolina Archery Products | | 2,114 | | 2,112 |
| Consolidation adjustment | | (805) | | (1,078) |
| | | ----- | | ----- |
| Pro forma net income | \$ | 6,189 | \$ | 9,895 |
| | | ===== | | ===== |
| Basic earning per share: | | | | |
| Excluding Carolina Archery Products acquisition | \$ | 0.38 | \$ | 0.68 |
| Carolina Archery Products | | 0.16 | | 0.16 |
| Consolidation adjustment | | (0.06) | | (0.08) |
| | | ----- | | ----- |
| Pro forma basic earnings per share | \$ | 0.48 | \$ | 0.76 |
| | | ===== | | ===== |

The consolidation adjustment in the above tables reflects the amortization of patents and other intangible assets over the expected economic lives.

Note K - Restructuring Costs

In 2004 the Company initiated a facility consolidation plan and involuntary employee terminations in the Office Products segment in order to reduce costs and increase the competitiveness of the Company. Under these plans no additional costs were incurred during the quarter ended October 7, 2006. Liabilities under these plans are as follows:

10

| (All amounts in thousands) | Balance at July 15, 2006 | Non-Cash Charges | Cash Payments | |
|-----------------------------|--------------------------------|---------------------|------------------|-------|
| | ----- | ----- | ----- | ----- |
| Severance and benefit costs | \$ 148 | \$ -- | \$ -- | \$ |
| Facility closure costs | -- | -- | -- | |
| | ----- | ----- | ----- | ----- |
| | \$ 148 | \$ -- | \$ -- | \$ |
| | ===== | ===== | ===== | ===== |

Note L - Reclassifications

Certain reclassifications have been made to the 2005 financial statements to conform to the 2006 financial statement presentation.

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

Forward-Looking Statements

This report contains forward-looking statements relating to present or future trends or factors that are subject to risks and uncertainties. These risks

Edgar Filing: ESCALADE INC - Form 10-Q

include, but are not limited to, the impact of competitive products and pricing, product demand and market acceptance, new product development, the continuation and development of key customer and supplier relationships, Escalade's ability to control costs, general economic conditions, fluctuation in operating results, changes in the securities market and other risks detailed from time to time in Escalade's filings with the Securities and Exchange Commission. Escalade's future financial performance could differ materially from the expectations of management contained herein. Escalade undertakes no obligation to release revisions to these forward-looking statements after the date of this report.

Overview

Escalade, Incorporated ("Escalade" or "Company") manufactures and distributes products for two industries: Sporting Goods and Office Products. Within these industries the Company has successfully built a commanding market presence in niche markets. This strategy is heavily dependent on brand recognition and excellent customer service. Management believes the key indicators in measuring the success of this strategy are revenue and earnings growth. A key strategic advantage is the Company's established relationships with major customers that allow the Company to bring new products to the market in a cost effective manner while maintaining a diversified product line and wide customer base. In addition to strategic customer relations, the Company has over 75 years of manufacturing and import experience that enable it to be a low cost supplier.

Results of Operations

Net revenues for the three months and nine months ended October 7, 2006 increased 3.2% and 4.6%, respectively, over the same periods last year. However, operating income for the three months and nine months ended October 7, 2006 declined 30.2% and 20.6%, respectively, as a result of lower gross margins and higher selling, general and administrative expenses. The following schedule sets forth certain consolidated statement of income data as a percentage of net revenue for the periods indicated:

11

| | Three Months ended | | |
|--|--------------------|--------------------|-----|
| | October 7, 2006 | October 1, 2005 | Oct |
| Net revenue | 100.0% | 100.0% | |
| Cost of products sold | 74.7% | 72.6% | |
| Gross margin | 25.3% | 27.4% | |
| Selling, administrative and general expenses | 16.2% | 14.1% | |
| Operating income | 9.1% | 13.3% | |

Consolidated Revenue and Gross Margin

Sporting Goods sales, compared to the same periods last year, increased 4.5% and 13.8% for the three months and nine months ended October 7, 2006, respectively. Excluding revenues from product lines acquired during the first half of fiscal 2006, revenues for the three months and nine months ended October 7, 2006 declined 5.7% and 0.6%, respectively. This decline reflects a timing delay in when some of the Company's largest mass market retailers accept stocking

Edgar Filing: ESCALADE INC - Form 10-Q

shipments for the holiday season. Assuming that holiday shopping results are in line with the expectations of the Company's mass market retailers, Management is cautiously optimistic that fiscal 2006 sales to mass market retailers, including large sporting goods chain retailers, will be roughly equal to the volume achieved in fiscal 2005. To lessen the impact of revenue fluctuations in mass market retailers, Management continues to pursue a strategy designed to expand distribution into the specialty sporting goods retailers and dealers.

Acquisitions in the first half of fiscal 2006 relating to archery accessories and residential playground systems directly support this strategy and have resulted in increased sales levels to this market segment of 34.8% and 18.0% for the three months and nine months ended October 7, 2006, respectively. Encouraged by success in the specialty retail and dealer market, Management believes total sporting goods revenues for fiscal 2006 will exceed the total achieved in fiscal 2005.

Office Product sales, compared to the prior year, were down 1.5% and 12.9% for the three months and nine months ended October 7, 2006, respectively. In the second half of 2005 the Company undertook a program of rationalizing low margin products and unprofitable customers. Excluding the effects of this rationalization on the third quarter, sales increased 1.0% over the same period last year. The effects of this rationalization program accounted for approximately one-third of the year-to-date sales decline. The remainder of the year to date sales decline is attributed to lower market demand for high security shredders and price competition in the European shredder market. The Company continues to invest in sales and marketing personnel that it believes is beginning to reverse the sales decline experienced year-to-date and expects to fully realize the benefits of this in early 2007. Consequently, Office products sales for 2006 are expected to be lower than 2005.

The overall gross margin for the three months and nine months ended October 7, 2006 were down from the same periods last year due primarily to the relative size of the two business segments. The overall gross margin will continue to decline as Sporting Goods, which has a lower gross margin than Office Products, becomes a larger proportion of total sales. The year-to-date gross margin in the Sporting Goods business has declined slightly compared to last year as a result of pricing pressures at mass market retail customers and unexpected manufacturing costs associated with the start-up of the new facility in Reynosa, Mexico. The rationalization of low margin products and the elimination of unprofitable customers in the Office Products business has yielded increased year-to-date gross margins compared to the same period last year. Rising oil prices could have a direct impact on raw material prices for steel and resin which constitute a significant portion of product costs in both business segments. To the extent that these cost increases cannot be passed on to customers, the gross margins in both business segments will be negatively impacted. At present it is not possible to quantify the extent or impact on future gross margins.

12

Consolidated Selling, General and Administrative Expenses

Consolidated selling, general and administrative expenses increased 19.2% and 14.7% in the three months and nine months ended October 7, 2006, respectively. Roughly 67.9% of the year-to-date increase relates to the Sporting Goods business which incurred non-recurring relocation costs in starting up the new manufacturing facility in Reynosa, Mexico and higher selling and advertising costs associated with new store display units in large retail customers. Excluding non-recurring costs the ratio of selling, general and administrative costs to revenues in the Sporting Goods business remain relatively unchanged from the prior year. However, the Sporting Goods business will experience higher selling and advertising costs as it expands its distribution into the specialty

Edgar Filing: ESCALADE INC - Form 10-Q

market; this should be balanced out with higher margins. Year-to-date selling, general and administrative costs in the Office Products business are slightly lower than the same period last year due to the lower sales volume. Unallocated corporate costs were higher due to expensing incentive stock options, roughly 18.1% of the overall total increase, and one-time non-recurring costs associated with the retirement of Mr. Reed, former President and CEO of the Company.

Provision for Income Taxes

The effective tax rate for the three months and nine months ended October 7, 2006 were significantly higher than the rates achieved in the same periods last year due to a one time adjustment to foreign taxes and losses in the Company's European operations where the Company does not receive a tax benefit. Management does not expect the overall effective tax rate to improve for the remainder of this year.

Net Income

Compared to last year, profitability in the Sporting Goods business was down in both the three months and nine months ended October 7, 2006 due to pricing pressures from mass market retailers and higher selling, general and administrative costs associated with expanding distribution in the specialty market channels. Profitability in the Office Products business was relatively unchanged compared to last year. Management expects earnings for fiscal 2006 to be lower than that achieved in fiscal 2005.

Financial Condition and Liquidity

The following schedule summarizes the Company's total debt:

| In thousands | October 7, 2006 | October 1, 2005 | D |
|--|--------------------|--------------------|----|
| Notes payable short-term | \$ 24,534 | \$ 10,590 | \$ |
| Current portion long-term debt | -- | -- | |
| Long term debt | 28,020 | 25,338 | |
| | ----- | ----- | |
| Total debt | \$ 52,554 | \$ 35,928 | \$ |
| | ===== | ===== | |
| | | | |
| Total debt as a percentage of stockholder's equity | 66.1% | 49.4% | |

Approximately 85.5% of the increase in total debt as of October 7, 2006 is attributed to the acquisitions completed by the Company during the first half of fiscal 2006. The balance of the increase is related to the payment of a dividend, stock purchased under the Company's stock buy-back plan, and funding operations.

During the nine months ended October 7, 2006, operations consumed \$2.6 million in cash compared to generating \$2.7 million for the same period last year reflecting slightly higher Sporting Goods inventories in the current year compared to the same time last year. Management believes the abnormally high inventory levels will be resolved by the end of fiscal 2006 and that no additional excess or obsolete reserves are necessary.

The Company's working capital requirements are primarily funded from operating cash flows and revolving credit agreements with its banks. The Company's relationship with its primary lending bank remains strong and the Company has

the same level of revolving credit that was available in 2005. Consequently, the Company believes it has sufficient credit to fund operations for the remainder of the year. The Company believes it can quickly reach agreement to increase available credit should the need arise.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is exposed to financial market risks, including changes in currency exchange rates, interest rates and marketable equity security prices. To mitigate these risks, the Company utilizes derivative financial instruments, among other strategies. At the present time, the only derivative financial instrument used by the company is an interest rate swap. The Company does not use derivative financial instruments for speculative purposes.

A substantial majority of revenue, expense and capital purchasing activities are transacted in U.S. dollars. However, the Company's foreign subsidiaries enter into transactions in other currencies, primarily the Euro. To protect against reductions in value and the volatility of future cash flows caused by changes in currency exchange rates, the Company carefully considers the use of transaction and balance sheet hedging programs. Such programs reduce, but do not entirely eliminate, the impact of currency exchange rate changes. Presently the Company does not employ currency exchange hedging financial instruments, but has adjusted transaction and cash flows to mitigate adverse currency fluctuations. Historical trends in currency exchanges indicate that it is reasonably possible that adverse changes in exchange rates of 20% for the Euro could be experienced in the near term. Such adverse changes would have resulted in a material impact on income before taxes for the nine months ended October 7, 2006.

A substantial portion of the Company's debt is based on U.S. prime and LIBOR interest rates. In an effort to mitigate the risk of unfavorable interest rate fluctuations the Company entered an interest rate swap agreement. This agreement effectively converted a portion of its variable rate debt into fixed rate debt.

An adverse movement of equity market prices would have an impact on the Company's long-term marketable equity securities that are included in other assets on the consolidated balance sheet. At October 7, 2006 the aggregate fair value of long-term marketable equity securities was \$2.6 million. Due to the unpredictable nature of the equity market the Company has not employed any hedge programs relative to these investments.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Escalade maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure based closely on the definition of "disclosure controls and procedures" in Rule 13a-14(c). In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit

Edgar Filing: ESCALADE INC - Form 10-Q

relationship of possible controls and procedures. Also, the Company has investments in certain unconsolidated entities. As the Company does not control or manage these entities, its disclosure controls and procedures with respect to such entities are necessarily substantially more limited than those it maintains with respect to its consolidated subsidiaries.

The Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and the Company's Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of the end of the period covered by this report. Based on the foregoing, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective.

14

Changes in Internal Control over Financial Reporting

Management of the Company has evaluated, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, changes in the Company's internal controls over financial reporting (as defined in Rule 13a-15(f) and 15d-15(f) of the Exchange Act) during the third quarter of 2006.

There have been no changes to the Company's internal control over financial reporting that occurred since the beginning of the Company's third quarter of 2006 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1 and 1.A. Not Required.

Item 2. (c) ISSUER PURCHASES OF EQUITY SECURITIES

| Period | (a) Total Number of Shares (or Units) Purchased | (b) Average Price Paid per Share (or Unit) | (c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs |
|---|---|--|---|
| Shares purchases prior to 07/15/2006 under the current repurchase program | 482,418 | \$ 9.46 | 482,438 |
| Third quarter purchases: | | | |
| 07/16/2006 - 08/12/2006 | None | None | None |
| 08/13/2006 - 09/09/2006 | None | None | None |
| 09/10/2006 - 10/07/2006 | None | None | None |

Edgar Filing: ESCALADE INC - Form 10-Q

| | | | | |
|---|---------|----|------|---------|
| Total share purchases under the current program | 482,418 | \$ | 9.46 | 482,438 |
|---|---------|----|------|---------|

The Company has one stock repurchase program which was established in February 2003 by the Board of Directors and which authorized management to expend up to \$3,000,000 to repurchase shares on the open market as well as in private negotiated transactions. The repurchase plan has no termination date. There have been no share repurchases that were not part of a publicly announced program. In February 2006, the Board of Directors increased the remaining amount on this plan to its original level of \$3,000,000.

Item 3, 4, and 5. Not Required.

15

Item 6. Exhibits

(a) Exhibits

| Number | Description |
|--------|--|
| 31.1 | Chief Executive Officer Rule 13a-14(a)/15d-14(a) Certification. |
| 31.2 | Chief Financial Officer Rule 13a-14(a)/15d-14(a) Certification. |
| 32.1 | Chief Executive Officer Section 1350 Certification. |
| 32.2 | Chief Financial Officer Section 1350 Certification. |
| 10.1 | Relocation and retention agreement dated July 24, 2006 by and between Escalade, Incorporated and Terry Frandsen. (Management Contract) (a) |

(a) Incorporated by reference from the Company's Form 8-K filed with the Securities and Exchange Commission on July 26, 2006.

SIGNATURE

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.

ESCALADE, INCORPORATED

Date: October 26, 2006

/s/ DANIEL A. MESSMER

Daniel A. Messmer
President and Chief Executive Officer

Date: October 26, 2006

/s/ TERRY D. FRANSDEN

Terry D. Frandsen
Vice President and Chief Financial Officer

