

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

NAUTICA ENTERPRISES INC
Form 10-Q
July 16, 2002

SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

FORM 10-Q

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended June 1, 2002 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 0-6708

Nautica Enterprises, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware

95-2431048

(State or Other Jurisdiction of Incorporation or Organization)

(I.R.S. Employer Identification No.)

40 West 57th Street, New York, N.Y.

10019

(Address of Principal Executive Offices)

(Zip Code)

Registrant's Telephone Number, including Area Code

(212) 541-5757

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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

APPLICABLE ONLY TO ISSUERS INVOLVED IN
BANKRUPTCY PROCEEDINGS DURING THE
PRECEDING FIVE YEARS

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Section 12, 13, or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.

Yes No
----- -----

APPLICABLE ONLY TO CORPORATE ISSUERS

The number of shares of Common Stock outstanding as of July 16, 2002 was 33,618,350.

NAUTICA ENTERPRISES, INC. AND SUBSIDIARIES JUNE 1, 2002 (unaudited)

INDEX

	Page No. -----
Part I - Financial Information:	
Item 1. Financial Statements (unaudited):	
Condensed Consolidated Balance Sheets As at June 1, 2002 and March 2, 2002	2
Condensed Consolidated Statements of Earnings For the Three Month Periods Ended June 1, 2002 and June 2, 2001	3
Condensed Consolidated Statements of Cash Flows For the Three Month Periods Ended June 1, 2002 and June 2, 2001	4
Notes to Condensed Consolidated Financial Statements	5
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	12
Item 3. Quantitative and Qualitative Disclosures About Market Risk	16
Part II - Other Information	17

NAUTICA ENTERPRISES, INC. AND SUBSIDIARIES CONDENSED CONSOLIDATED BALANCE SHEETS

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

(amounts in thousands, except share data)

ASSETS	(unaudited) June 1, 2002 -----	March 2, 2002 -----
Current assets:		
Cash and cash equivalents	\$ 74,061	\$ 45,814
Short-term investments	6,794	6,350
Accounts receivable - net	64,453	89,736
Inventories	63,648	66,443
Prepaid expenses and other current assets	7,660	5,599
Deferred tax benefit	18,858	18,912
Assets held for sale	2,842	2,842
Total current assets	----- 238,316	----- 235,696
Property, plant and equipment, at cost - less accumulated depreciation and amortization	109,078	111,327
Goodwill, at cost - less accumulated amortization	31,328	31,328
Intangibles, at cost - less accumulated amortization	35,419	35,489
Other assets	10,095	8,230
	----- \$ 424,236 =====	----- \$ 422,070 =====
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Current maturities of long-term debt	\$ 754	\$ 754
Accounts payable - trade	32,440	30,402
Accrued expenses and other current liabilities	46,921	44,037
Income taxes payable	7,453	9,289
Total current liabilities	----- 87,568	----- 84,482
Long-term liabilities:		
Long-term debt - net	14,133	14,321
Interest rate swap liability	858	687
Total long-term liabilities	----- 14,991	----- 15,008
Stockholders' equity:		
Preferred stock - par value \$.01; authorized, 2,000,000 shares; no shares issued	--	--
Common stock - par value \$.10; authorized, 100,000,000 shares; issued 45,115,000 shares at June 1, 2002 and 44,718,000 shares at March 2, 2002	4,512	4,472
Additional paid-in capital	95,162	93,546
Retained earnings	382,782	385,407
Accumulated other comprehensive (loss) - net of deferred tax benefit of \$1,078 at June 1, 2002 and \$1,132 at March 2, 2002	(1,796)	(1,862)
	----- 480,660	----- 481,563

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

Less:

Common stock in treasury, at cost;
11,498,000 shares at June 1, 2002
and March 2, 2002

	(158,983)	(158,983)
	-----	-----
Total stockholders' equity	321,677	322,580
	-----	-----
	\$ 424,236	\$ 422,070
	=====	=====

The accompanying notes are an integral part of these statements.

- 2 -

NAUTICA ENTERPRISES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS
(amounts in thousands, except share data)

	(unaudited)	
	Three Months Ended June 1, 2002	Three Months Ended June 2, 2002
	-----	-----
Net sales	\$ 125,895	\$ 135,895
Cost of goods sold	70,161	77,161
	-----	-----
Gross profit	55,734	57,734
Selling, general and administrative expenses	59,626	55,626
Special charges	3,356	3,356
Net royalty income	(2,372)	(2,372)
	-----	-----
Operating (loss) profit	(4,876)	4,876
Investment income - net	677	677
	-----	-----
(Loss) earnings before (benefit) provision for income taxes	(4,199)	5,199
(Benefit) provision for income taxes	(1,574)	1,574
	-----	-----
NET (LOSS) EARNINGS	\$ (2,625)	\$ 3,625
	=====	=====
Net (loss) earnings per share of common stock:		
Basic	\$ (0.08)	\$ 0.08
	=====	=====
Diluted	\$ (0.08)	\$ 0.08
	=====	=====

Weighted average number of common shares outstanding:

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

Basic	33,432,000	32,259,
	=====	=====
Diluted	33,432,000	34,025,
	=====	=====
Cash dividends per common share	none	n
	=====	=====

The accompanying notes are an integral part of these statements.

- 3 -

NAUTICA ENTERPRISES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(amounts in thousands)

	(u Three Month Ended June 1, 200

CASH FLOWS FROM OPERATING ACTIVITIES	
Net (loss) earnings	\$ (2,625)

Adjustments to reconcile net (loss) earnings to net cash provided by operating activities:	
Deferred income taxes	--
Depreciation and amortization	6,651
Provision for bad debts	128
Changes in operating assets and liabilities, net of assets and liabilities acquired	
Short-term investments	(444)
Accounts receivable	25,155
Inventories	2,795
Prepaid expenses and other current assets	(2,061)
Other assets	(1,891)
Accounts payable - trade	2,038
Accrued expenses and other current liabilities	3,174
Income taxes payable	(1,836)

Total adjustments	33,709

Net cash provided by operating activities	31,084

CASH FLOWS FROM INVESTING ACTIVITIES	
Purchase of property, plant and equipment	(4,305)
Acquisitions, net of cash acquired	--

Net cash (used in) investing activities	(4,305)

CASH FLOWS FROM FINANCING ACTIVITIES	
Proceeds from notes payable	--
Principal payments on long-term debt	(188)
Proceeds from issuance of common stock	1,656

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

Net cash provided by financing activities	1,468

Increase (decrease) in cash and cash equivalents	28,247
Cash and cash equivalents at beginning of period	45,814

Cash and cash equivalents at end of period	\$ 74,061

Supplemental disclosure of cash flow information:	
Cash paid during the period for interest	\$ 315

Cash paid during the period for income taxes	\$ 219

The accompanying notes are an integral part of these statements.

- 4 -

NAUTICA ENTERPRISES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
JUNE 1, 2002
(unaudited)
(amounts in thousands, except share data)

- NOTE 1 - The accompanying financial statements have been prepared without audit pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. These statements include all adjustments, consisting only of normal recurring accruals, considered necessary for a fair presentation of financial position and results of operations. The financial statements included herein should be read in conjunction with the financial statements and notes thereto included in the latest annual report on Form 10-K.
- NOTE 2 - The results of operations for the three-month period ended June 1, 2002 are not necessarily indicative of the results to be expected for the full year.
- NOTE 3 - Certain amounts in the prior year period have been reclassified to conform with classifications used at June 1, 2002.
- NOTE 4 - The Company utilized the last-in, first-out "LIFO" method for certain wholesale inventories as at June 1, 2002 and March 2, 2002 and for the three-month periods ended June 1, 2002 and June 2, 2001. The "LIFO" inventory for the three-month periods ended June 1, 2002 and

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

June 2, 2001 are based upon end of year estimates. Inventories at June 1, 2002 and March 2, 2002 consist primarily of finished goods.

NOTE 5 - As of June 1, 2002 and March 2, 2002, the Company had \$175,000 in lines of credit with four commercial banks. Such lines of credit are available for short-term borrowings and letters of credit, collateralized by imported inventory and accounts receivable. At June 1, 2002, letters of credit outstanding under the lines were \$75,597. At June 1, 2002 and March 2, 2002, there were no short-term borrowings outstanding.

NOTE 6 - Basic net (loss) earnings per share excludes dilution and is computed by dividing the (loss) income available to common shareholders by the weighted-average common shares outstanding for the period. Diluted net (loss) earnings per share reflects the weighted-average common shares outstanding plus the potential dilutive effect of options, which are convertible into common shares. The diluted net loss per share was the same as basic net loss per share for the three months ended June 1, 2002, since the effect of any potentially dilutive securities were excluded because they would be anti-dilutive. Options, which were excluded from the calculation of diluted net loss per share, totaled 2,612,300 for the three months ended June 1, 2002. Options which were excluded from the calculation of diluted net earnings per share because the exercise prices of the options were greater than the average market price of the common shares and, therefore, would be anti-dilutive, were 2,198,900 during the three months ended June 2, 2001.

- 5 -

NAUTICA ENTERPRISES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
JUNE 1, 2002
(unaudited)
(amounts in thousands, except share data)

NOTE 7 - The Company has adopted Statement of Financial Accounting Standards ("SFAS") No. 131, "Disclosures about Segments of an Enterprise and Related Information," which establishes reporting and disclosure standards for an enterprise's operating segments. Operating segments are defined as components of an enterprise for which separate financial information is available and regularly reviewed by the Company's senior management.

The Company has the following two reportable segments: Wholesale and Retail. The Wholesale segment designs, markets, sources and distributes the following to retail store customers: sportswear, activewear, outerwear, a jeans collection, a tailored clothing collection, robes and sleepwear for men; a jeans collection, robes and sleepwear for women; and a children's collection. The Retail segment sells men's, women's and children's apparel and other Nautica-branded products primarily through its retail store locations directly to consumers.

The reportable segments are distinct business units, separately managed with different distribution channels.

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

	Wholesale -----	Retail -----	All other -----	Corporate/ eliminations -----	T
FOR THE THREE MONTHS ENDED JUNE 1, 2002					
Net sales	\$ 95,337	\$ 30,558	\$ --	\$ --	\$ 1
Segment operating profit (loss)	(626)	225	2,372	(6,847)	4
Segment assets	254,301	49,717	8,673	111,545	4
Depreciation expense	5,144	731	106	573	
Capital expenditures	3,916	254	--	135	
FOR THE THREE MONTHS ENDED JUNE 2, 2001					
Net sales	\$ 105,017	\$ 30,173	\$ --	\$ --	\$ 1
Segment operating profit (loss)	2,256	2,393	2,344	(2,164)	4
Segment assets	322,962	69,201	8,687	42,189	4
Depreciation expense	4,706	330	107	513	
Capital expenditures	11,095	5,193	--	1,191	

Net sales from external customers represent sales in the United States, except for foreign sales of \$1,009 and \$1,970 for the three months ended June 1, 2002 and June 2, 2001, respectively

Long-lived assets in foreign countries were \$3,168 and \$4,548 for the periods ended June 1, 2002 and June 2, 2001, respectively.

The All other column represents activity of the Company's licensing unit.

- 6 -

NAUTICA ENTERPRISES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
JUNE 1, 2002
(unaudited)
(amounts in thousands, except share data)

In the Corporate/eliminations column, the segment assets primarily consist of the Company's cash and investment portfolio at June 1, 2002 and June 2, 2001. The segment operating profit (loss) in the Corporate/eliminations column consists of corporate overhead expenses and special charges for the three months ended June 1, 2002 and corporate overhead expenses for the three months ended June 2, 2001.

NOTE 8 -

The Company has a loan agreement with HSBC Bank USA ("HSBC") in the amount of \$15,075, the funds of which were used to finance a portion of the construction and development of the Company's distribution facility in Martinsville, Virginia. The loan is secured by a deed of trust on the distribution facility. The carrying value of the underlying asset was \$18,042 at June 1, 2002.

The term of the loan is seven years. Principal payments of \$188 and interest payments are due at the end of

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

each calendar quarter. Interest is computed based on the three-month LIBOR rate plus 1.00%. The loan agreement provides for various financial and restrictive covenants including, among others, tangible net worth, minimum fixed charges and minimum funded debt. The loan will mature on November 28, 2008, at which time the entire outstanding loan balance of \$9,987 will be due and payable.

The Company entered into a swap agreement with HSBC, effective November 30, 2001, to hedge against interest rate fluctuations. On March 22, 2002, the Company replaced such agreement with a "knock-out" swap agreement with Fleet National Bank ("Fleet"), which expires on November 28, 2008. The swap settles quarterly and contains a knock-out provision that is activated when the three-month LIBOR is at or above 7.00%. The swap agreement provides that the Company pay a fixed interest rate of 6.32% on the notional amount in exchange for receiving a variable rate based on LIBOR so long as the three-month LIBOR interest rate does not rise above 7.00%. If the three-month LIBOR rate rises above 7.00%, the swap knocks out and the Company will not receive any payments under the agreement until such time as the three-month LIBOR rate declines below 7.00%. The three-month LIBOR rate was 1.86% at June 1, 2002. The net interest paid or received under this agreement is included in interest expense.

The Company has adopted SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended, which requires companies to record all derivative instruments as assets or liabilities on the balance sheet, measured at fair value. The recognition of gains or losses resulting from changes in the values of those derivative instruments is based on the use of each derivative instrument and whether it qualifies for hedge accounting. The key criterion for hedge accounting is that the hedging relationship must be highly effective in achieving offsetting changes in fair value or cash flows.

- 7 -

NAUTICA ENTERPRISES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
JUNE 1, 2002
(unaudited)
(amounts in thousands, except share data)

Prior to March 22, 2002 the Company classified the swap as a cash flow hedge, in accordance with SFAS No. 133. The fair value of the swap resulted in the Company recording a long-term liability of \$858. The fair value is based upon the estimated amount that the Company would have to pay to terminate the agreement, as determined by HSBC at March 22, 2002 and Fleet at June 1, 2002. The "knock-out" swap agreement no longer qualifies for hedge accounting and the Company began recording the changes in the fair market value of the swap from March 22, 2002 as interest expense. The charge to interest expense for the quarter ended June 1, 2002 was not material.

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

The amount of long-term debt maturing in each of the next five fiscal years is as follows:

Fiscal Year Ended		

2003	\$	754
2004		754
2005		754
2006		754
2007		754
Thereafter		11,305

		14,887
Less current maturities		(754)

Total	\$	14,133
		=====

NOTE 9 - For the three months ended June 1, 2002, comprehensive income (loss) was as follows:

	(unaudited) Three Months Ended June 1, 2002 -----
Net (loss)	\$(2,625)
Other comprehensive (loss), net of taxes:	
Foreign currency translation adjustments	175
Unrealized loss on interest rate swap	(109)

Comprehensive income (loss)	\$(2,559)
	=====

- 8 -

NAUTICA ENTERPRISES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
JUNE 1, 2002
(unaudited)
(amounts in thousands, except share data)

NOTE 10 - On November 2, 2001, the Company's Board of Directors adopted a Stockholder Rights Plan that entitled stockholders of record on November 12, 2001 to receive a dividend distribution of one Right for each share of common stock held.

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

The Rights, which expire on November 12, 2011, entitle stockholders to purchase from the Company a unit consisting of 1/100 of a share of Series A Junior Participating Preferred Stock at a price of \$60 per unit, subject to adjustment. The Rights will become exercisable only if a person or group, other than the current Chairman of the Board, acquires 15% or more of the Company's common stock.

NOTE 11 -

In July 2001, the Financial Accounting Standards Board issued SFAS No. 142, "Goodwill and Other Intangible Assets." This statement requires that goodwill, as well as intangible assets with indefinite lives, acquired after June 30, 2001, will not be amortized. Effective in the first quarter of the current year, goodwill and intangible assets with indefinite lives are no longer being amortized, but are being tested for impairment using the guidance for measuring impairment set forth in this statement.

The components of other intangible assets are as follows:

	(unaudited)		March 2, 2002	
	June 1, 2002	June 1, 2002	March 2, 2002	March 2, 2002
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
	-----	-----	-----	-----
Amortized Intangible Assets				
Trademarks	\$ 2,341	\$ 1,147	\$ 2,327	\$ 1,063
Other intangibles	956	258	956	258
	-----	-----	-----	-----
	3,297	1,405	3,283	1,321
Unamortized trademarks	33,527	--	33,527	--
	-----	-----	-----	-----
	\$36,824	\$ 1,405	\$36,810	\$ 1,321
	=====	=====	=====	=====

Amortization expense for intangible assets subject to amortization in each of the next five fiscal years is estimated to be \$562 in 2003, \$527 in 2004, \$527 in 2005, \$423 in 2006 and \$351 in 2007.

- 9 -

NAUTICA ENTERPRISES, INC. AND SUBSIDIARIES
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
 JUNE 1, 2002
 (unaudited)
 (amounts in thousands, except share data)

The following presents a comparison of net (loss) earnings and (loss) earnings per share for the three months ended June 1, 2002 to the respective adjusted amounts for the three months ended June 2, 2001 that would have been

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

reported had SFAS No. 142 been in effect during the prior year:

	(unaudited) June 1, 2002 -----	(unaudited) June 2, 2001 -----
Reported net (loss) earnings	\$ (2,625)	\$ 3,173
Goodwill amortization	--	202
Intangible assets amortization	--	146
	-----	-----
Adjusted net (loss) earnings	\$ (2,625) =====	\$ 3,521 =====
Net (loss) earnings per share - basic		
Reported net (loss) earnings	\$ (0.08)	\$ 0.10
Goodwill amortization	--	0.01
Intangible assets amortization	--	--
	-----	-----
Adjusted net (loss) earnings per share - basic	\$ (0.08) =====	\$ 0.11 =====
Net (loss) earnings per share - diluted		
Reported net (loss) earnings	\$ (0.08)	\$ 0.09
Goodwill amortization	--	0.01
Intangible assets amortization	--	--
	-----	-----
Adjusted net (loss) earnings per share - diluted	\$ (0.08) =====	\$ 0.10 =====

NOTE 12- During the fourth quarter of fiscal 2002, the Company recorded special charges in connection with its decision to close its distribution facility in Rockland, Maine and certain other employee terminations. The Company will be moving the businesses that currently use this facility to its new distribution and customer service center in Martinsville, Virginia. This transition is expected to be completed no later than January 31, 2003. The special charges related to the closing will total approximately \$13,159, of which \$9,803 was recognized in the fourth quarter of fiscal 2002 and \$3,356 was recognized in the first quarter of fiscal 2003. The special charges are comprised of the write-down of the facility from its net carrying value of \$10,712 to its estimated net realizable value of \$2,842, costs associated with the closure and sale of the facility and severance related costs associated with the elimination of approximately 300 union and non-union employees and certain other employee terminations. These components and the related activity through June 1, 2002 were as follows:

- 10 -

NAUTICA ENTERPRISES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
JUNE 1, 2002
(unaudited)
(amounts in thousands, except share data)

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

	ASSET WRITE DOWN -----	WIND DOWN COSTS -----	SEVERANCE AND TERMINATION BENEFITS -----	TOTALS -----
Fiscal Year 2002 Provision	\$ 7,870	\$ 868	\$ 1,065	\$ 9,803
Fiscal Year 2002 Activity	(7,870)	--	--	(7,870)
	-----	-----	-----	-----
Balance at March 2, 2002	--	868	1,065	1,933
Fiscal Year 2003 Provision	--	--	3,356	3,356
Fiscal Year 2003 Activity	--	(150)	(524)	(674)
	-----	-----	-----	-----
Balance at June 1, 2002	\$ --	\$ 718	\$ 3,897	\$ 4,615
	=====	=====	=====	=====

NOTE 13 - Effective March 3, 2002, the Company adopted Financial Accounting Standards Board's ("FASB") Emerging Issues Task Force Issue No. 01-9, "Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)." The scope of Issue 01-9 includes vendor consideration to any purchasers of the vendor's products at any point along the distribution chain, regardless of whether the purchaser receiving the consideration is a direct customer of the vendor. There was no significant impact on the financial statements upon adoption.

Effective March 3, 2002, the Company adopted SFAS No. 142, "Goodwill and Other Intangible Assets." Under SFAS No. 142, goodwill and intangible assets with indefinite lives are no longer amortized but will be reviewed at least annually for impairment. Separable intangible assets that are not deemed to have an indefinite life will continue to be amortized over their useful lives. The Company completed the first of the required impairment tests of goodwill during the three months ended June 2, 2002 and no adjustment to the carrying value of goodwill was required.

Effective March 3, 2002 the Company adopted SFAS No. 144, "Accounting for the Impairment or Disposal of Long Lived Assets." This supercedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long Lived Assets to be Disposed of," while retaining many of the requirements of such statement. There was no significant impact on the financial statements upon adoption.

The FASB issued SFAS No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections," on April 30, 2002. Statement No. 145 rescinds Statement No.4, which required all gains and losses from extinguishments of debt to be aggregated and, if material, classified as an extraordinary item, net of related income tax effect. Upon adoption of Statement No. 145, companies will be required to apply the criteria in APB Opinion No. 30, "Reporting the Results of Operations - reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions" in determining the classification of gains and losses resulting from the extinguishments of debt. Statement No. 145 is effective for fiscal years beginning after May

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

15, 2002. We are currently evaluating the requirements and impact of this statement on our consolidated results of operations and financial position.

- 11 -

ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (unaudited)

RESULTS OF OPERATIONS

For the Three Months Ended June 1, 2002:

Net sales decreased 6.9% to \$125.9 million in the three months ended June 1, 2002 from \$135.2 million in the comparable prior year period. The reported sales reflect a 9.2% decrease in the Wholesale segment to \$95.3 million from \$105.0 million and a 1.3% increase in the Retail segment to \$30.6 million from \$30.2 million. The decline in the Wholesale segment was due primarily to a decrease in the Company's core sportswear business, offset by strong performances of Nautica Men's and Women's Jeans, as well as contributions from newer businesses including Earl Jean and Nautica Men's Underwear. The increase in Retail segment sales is primarily a result of sales from three new outlet stores and two full-price stores opened since the first quarter of last year. Same store sales for the period were down mid-single digits from the comparable prior year period, as a result of a difficult retail environment.

Gross profit, as a percentage of sales, was 44.3%, compared to 42.7% in the comparable prior year period. The increase is due primarily to the Company's inventory management initiatives, improved sourcing of the Nautica Children's and Nautica Men's and Women's Jeans businesses, and the impact of higher margins on certain new product lines, particularly Earl Jean.

Selling, general and administrative expenses ("SG&A") increased by \$4.3 million to \$59.6 million in Fiscal 2003 from \$55.3 million in Fiscal 2002. SG&A expenses, as a percentage of net sales, increased to 47.4% in Fiscal 2003 from 40.9% in Fiscal 2002. The increase as a percentage of net sales is due primarily to investments in Earl Jean Women's and Men's businesses, the development of the Nautica Women's Sportswear line and the expansion of the John Varvatos business into the European market. In addition, the Company incurred a full quarter of expenses from the Earl Jean business in the current period as opposed to only one month in the comparable prior year period.

During the first quarter of fiscal 2003, the Company recorded a pre-tax special charge of \$3.4 million (\$2.1 million on an after tax basis) or \$0.06 on a per share basis. This charge consists of costs associated with the elimination of approximately 300 union and non-union employees related to the closing of the Rockland, Maine distribution facility. These costs are expected to be paid during the current fiscal year and are anticipated to be funded with cash from operations. The Company expects annual savings associated with this action to be between \$4.0 and \$5.0 million. These savings will be reflected in distribution costs and reported in selling, general and administrative expenses in the Company's consolidated financial statements. The Company expects to begin realizing these cost savings in the fourth quarter of the current fiscal year.

Net royalty income remained essentially flat at \$2.4 million in comparison to the prior year period. Sales strength in home products during the current year period were offset in part by the recognition of a settlement from the termination of the men's footwear license during the comparable prior year period.

Investment income, net of interest expense, increased by \$0.4 million

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

to \$0.7 million from \$0.3 million in the prior year period. The increase is due to investment income earned on higher average cash balances during the current year period, as a result of cash paid during the prior year period for the acquisition of Earl Jean.

The provision for income taxes decreased to 37.5% from 37.8% of earnings before income taxes in the comparable prior year period. The decrease is due primarily to a reduction in the overall effective income tax rates.

Net loss for the current year period was \$2.6 million compared to net earnings of \$3.2 million in the comparable prior year period as a result of the factors discussed above. Excluding the special charge, the net loss for the current year period would have been \$0.5 million.

- 12 -

LIQUIDITY AND CAPITAL RESOURCES

During the three months ended June 1, 2002, the Company generated cash from operating activities of \$31.1 million, principally from a decrease in accounts receivable of \$25.2 million. Accounts receivable was 26.3% lower than the same period in the prior year due mainly to the reduction in wholesale shipments in the current year period. Inventory was \$61.3 million or 49.1% lower than the same period in the prior year due to the Company's ability to better manage the timing of receipts with customer demand as well as a reduction in its offerings of replenishment styles.

During the three months ended June 2, 2001, the Company generated cash from operating activities of \$8.0 million principally from net earnings. The increase in inventory of \$16.7 million, to support increased sales levels, was financed principally by cash generated from net earnings and a decrease of \$21.4 million in accounts receivable. Accounts receivable was 30.8% higher than the same period in the prior year due to increased sales from our new businesses, and the timing of shipments, with a higher percentage occurring in the last part of the quarter. Inventory was 43.4% higher than the same period in the prior year due primarily to increased sales and the timing of merchandise received to support the new businesses and stores.

During the three months ended June 1, 2002, the Company's principal investing activities related primarily to the purchase of property, plant and equipment for the Nautica in-store shop program. The Company expects to continue to incur capital expenditures to expand the in-store shop program, and to open additional retail stores.

The Company has a total of \$175.0 million in lines of credit with four commercial banks available for short-term borrowings and letters of credit. These lines are collateralized by imported inventory and accounts receivable. At June 1, 2002 and March 2, 2002, letters of credit outstanding under the lines were \$75.6 million and \$33.8 million, respectively, and there were no short-term borrowings outstanding.

The following is a summary of the Company's contractual obligations for the periods indicated that existed as of June 1, 2002:

(amounts in millions)					
Contractual Obligations	Less than 1 Year	1 - 3 Years	4 - 5 Years	After 5 Years	Total
-----	-----	-----	-----	-----	-----

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

Operating leases	\$ 17.3	\$ 32.4	\$ 29.3	\$ 67.5	\$146.5
Letters of credit	75.6	--	--	--	75.6
Long-term debt	0.8	1.5	1.5	11.1	14.9
	-----	-----	-----	-----	-----
	\$ 93.7	\$ 33.9	\$ 30.8	\$ 78.6	\$237.0
	=====	=====	=====	=====	=====

Historically, the Company has experienced its highest level of sales in the second and third quarters and its lowest level in the first and fourth quarters due to seasonal patterns. In the future, the timing of seasonal shipments may vary by quarter. The Company anticipates that internally generated funds from operations, existing cash balances, short-term investments and the Company's existing credit lines will be sufficient to satisfy its cash requirements.

- 13 -

CURRENCY FLUCTUATIONS AND INFLATION

The Company contracts production with manufacturers located primarily in Asia. These contracts are denominated in United States dollars. The Company believes that, to date, the effect of fluctuations of the dollar against foreign currencies has not had a material effect on the cost of production or the Company's results of operations. There can be no assurance that costs for the Company's products will not be affected by future fluctuations in the exchange rate between the United States dollar and the local currencies of these manufacturers. Due to the number of currencies involved, the Company cannot quantify the potential effect of such future fluctuations on future income. The Company does not engage in hedging activities with respect to such exchange rate risk.

The Company believes that inflation and the effect of fluctuations of the dollar against foreign currencies have not had a material effect on the cost of imports or the Company's results of operations.

NEW ACCOUNTING PRONOUNCEMENTS

Effective March 3, 2002, the Company adopted Financial Accounting Standards Board's ("FASB") Emerging Issues Task Force Issue No. 01-9, "Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)." The scope of Issue 01-9 includes vendor consideration to any purchasers of the vendor's products at any point along the distribution chain, regardless of whether the purchaser receiving the consideration is a direct customer of the vendor. There was no significant impact on the financial statements upon adoption.

Effective March 3, 2002, the Company adopted Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets." Under SFAS No. 142, goodwill and intangible assets with indefinite lives are no longer amortized but will be reviewed at least annually for impairment. Separable intangible assets that are not deemed to have an indefinite life will continue to be amortized over their useful lives. The Company completed the first of the required impairment tests of goodwill during the three months ended June 2, 2002 and no adjustment to the carrying value of goodwill was required.

Effective March 3, 2002 the Company adopted SFAS No. 144, "Accounting for the Impairment or Disposal of Long Lived Assets." This supercedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long Lived Assets to be Disposed of," while retaining many of the requirements of such

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

statement. There was no significant impact on the financial statements upon adoption.

The FASB issued SFAS No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections," on April 30, 2002. Statement No. 145 rescinds Statement No.4, which required all gains and losses from extinguishments of debt to be aggregated and, if material, classified as an extraordinary item, net of related income tax effect. Upon adoption of Statement No. 145, companies will be required to apply the criteria in APB Opinion No. 30, "Reporting the Results of Operations - reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions" in determining the classification of gains and losses resulting from the extinguishments of debt. Statement No. 145 is effective for fiscal years beginning after May 15, 2002. We are currently evaluating the requirements and impact of this statement on our consolidated results of operations and financial position.

- 14 -

USE OF ESTIMATES AND CRITICAL ACCOUNTING POLICIES

The Company's consolidated financial statements are prepared in accordance with accounting principles that are generally accepted in the United States. The preparation of these consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and revenues and expenses during the period. Management continually evaluates its estimates and assumptions including those related to allowances for doubtful accounts, sales returns and allowances, inventory valuation, accrual for markdowns and the valuation of long-lived assets. Management bases its estimates and assumptions on historical experience and other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. Changes in the economic conditions in the retail industry could have an impact on these estimates and the Company's actual results. Management believes that the following may involve a higher degree of judgment or complexity:

Allowances for Doubtful Accounts

In the normal course of business, the Company extends credit, on open account, to its retail store customers, after a credit analysis based on financial and other criteria. The Company maintains allowances for doubtful accounts for estimated losses that result from the inability of its retail store customers to make their required payments. Management bases its allowances through analysis of the aging of accounts receivable at the date of the financial statements, assessments of historical collection trends, and an evaluation of the impact of current economic conditions.

Sales Returns and Allowances

Costs associated with potential returns of merchandise and charge backs are recorded as a reduction to net sales, and are included in the allowance for doubtful accounts. These costs are based upon known returns and allowances, historic trends and the evaluation of the impact of current economic conditions.

Inventory Valuation

Inventories are stated at the lower of cost or market. Cost is determined by the last-in, first-out method for certain wholesale inventories and by the first-in, first-out method for retail and the remaining wholesale inventories. The Company marks down inventory for estimated unmarketable

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

inventory equal to the difference between the cost and the estimated net realizable value of the inventory. Management continually assesses the valuation of inventories by reviewing the costing of inventory, the significance of slow-moving inventory, and the impact of current economic conditions.

Accrual for Markdowns

Costs associated with customer markdowns are recorded as a reduction to net sales, and are included in the allowance for doubtful accounts. These costs result from seasonal negotiations with the Company's retail store customers, as well as historic trends and the evaluation of the impact of current economic conditions.

Valuation of Long-lived Assets

The Company reviews long-lived assets and certain identifiable intangibles held and used for possible impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. In evaluating the fair value and future benefits of such assets, the Company performs an analysis of the anticipated undiscounted future net cash flows of the individual assets over the remaining amortization period. The Company recognizes an impairment loss if the carrying value of the asset exceeds the expected future cash flows.

- 15 -

FORWARD-LOOKING AND CAUTIONARY STATEMENTS

Certain statements in this Form 10-Q and in future filings by the Company with the Securities and Exchange Commission, in the Company's press releases, and in oral statements made by or with the approval of authorized personnel constitute "forward-looking statements" as defined in the Private Securities Litigation Reform Act of 1995. These statements are based on the Company's current expectations of future events and are subject to a number of risks and uncertainties that may cause the Company's actual results to differ materially from those described in the forward-looking statements. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those anticipated, estimated or projected. These factors and uncertainties include, among others: the risk that new businesses of the Company will not be integrated successfully; the risk that the Company will experience difficulties with respect to the transitioning and ramp-up of its new distribution facility; the overall level of consumer spending on apparel; dependence on sales to a limited number of large department store customers; risks related to extending credit to customers; actions of existing or new competitors and changes in economic or political conditions in the markets where the Company sells or sources its products; risks associated with consolidations, restructuring and other ownership changes in the retail industry; changes in trends in the market segments in which the Company competes; risks associated with uncertainty relating to the Company's ability to launch, support and implement new product lines in the United States and Europe; effects of competition; changes in the costs of raw materials, labor and advertising; and, the ability to secure and protect trademarks and other intellectual property rights. These and other risks and uncertainties are disclosed from time to time in the Company's filings with the Securities and Exchange Commission, including the Company's periodic reports on Forms 10-K and 10-Q, the Company's press releases and in oral statements made by or with the approval of authorized personnel. The Company assumes no obligation to update any forward-looking statements as a result of new information or future events or developments.

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Disclosure about interest rate risk

The Company finances its capital needs through available capital, future earnings, bank lines of credit and its long-term debt which totals \$14.9 million, inclusive of its current portion. The Company's exposure to market risk for changes in interest rates are primarily in its investment portfolio and its short and long-term borrowings. The Company, pursuant to investing guidelines, mitigates exposure on its investments by limiting maturity, placing investments with high credit quality issuers and limiting the amount of credit exposure to any one issuer. All of the Company's indebtedness, including borrowings under its \$175 million lines of credit and long-term debt, bear interest at variable rates. Accordingly, changes in interest rates would impact the Company's results of operations in future periods. On March 22, 2002, the Company entered into a "knock-out" swap agreement with Fleet National Bank ("Fleet"), which expires on November 28, 2008. The swap settles quarterly and contains a knock-out provision that is activated when the three-month LIBOR is at or above 7.00%. The swap agreement provides that the Company pay a fixed interest rate of 6.32% on the notional amount in exchange for receiving a variable rate based on LIBOR so long as the three-month LIBOR interest rate does not rise above 7.00%. If the three-month LIBOR rate rises above 7.00%, the swap knocks out and the Company will receive no payments under the agreement until such time as the three-month LIBOR rate declines below 7.00%. The three-month LIBOR rate was 1.86% at June 1, 2002. The net interest paid or received under this agreement is included in interest expense.

- 16 -

PART II

OTHER INFORMATION

Items 1 through 9. - All items are inapplicable except:

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibit Index

Exhibit No.

- 3(a) Registrant's By-laws as currently in effect are incorporated herein by reference to Registrant's Registration Statement on Form S-1 (Registration No. 33-21998).
- 3(b) Registrant's Restated Certificate of Incorporation is incorporated herein by reference from the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended August 31, 1995, as amended by a Certificate of Amendment incorporated herein by reference from the Registrant's Quarterly Report on Form 10-Q for the quarter ended May 31, 1996.
- 3(c) Certificate of Designations of Series A Junior Participating Preferred Stock of Nautica Enterprises, Inc., in the form as filed with the Secretary of State of the State of Delaware,

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

included as Exhibit A to the Rights Agreement, dated as of November 2, 2001, between Nautica Enterprises, Inc. and Mellon Investor Services LLC, as Rights Agent, is incorporated herein by reference from the Registrant's Current Report on Form 8-K filed on November 8, 2001.

- 4(i) (a) Rights Agreement, dated as of November 2, 2001, between Nautica Enterprises, Inc. and Mellon Investor Services LLC, as Rights Agent, which includes the Certificate of Designations of Series A Junior Participating Preferred Stock as Exhibit A, form of Right Certificate as Exhibit B and the Summary of Rights to Purchase Preferred Stock as Exhibit C, is incorporated herein by reference from the Registrant's Current Report on Form 8-K filed on November 8, 2001.
- 10(iii) (a) Registrant's Executive Incentive Stock Option Plan is incorporated herein by reference from the Registrant's Registration Statements on Form S-8 (Registration Number 33-1488), as amended by the Company's Registration Statement on Form S-8 (Registration Number 33-45823).
- 10(iii) (b) Registrant's 1989 Employee Incentive Stock Plan is incorporated herein by reference from the Registrant's Registration Statement on Form S-8 (Registration Number 33-36040).
- 10(iii) (c) Registrant's 1996 Stock Incentive Plan is incorporated herein by reference from Registrant's Registration Statement on Form S-8 (Registration Number 333-55711), as amended and restated in Appendix A to the Registrant's Definitive Proxy Statement filed on June 7, 2002.
- 17 -
- 10(iii) (d) Registrant's 1994 Incentive Compensation Plan is incorporated herein by reference from the Registrant's Annual Report on Form 10-K for the fiscal year ended February 28, 1997.
- 10(iii) (e) Registrant's Deferred Compensation Plan is incorporated herein by reference from the Registrant's Annual Report on Form 10-K for the fiscal year ended February 28, 1998.
- 10(iii) (f) Option Agreement and Royalty Agreement, each dated July 1, 1987, by and among the Registrant and David Chu are incorporated herein by reference from the Registrant's Registration Statement on Form S-1 (Registration No. 33-21998), and letter agreement dated May 1, 1998 between Mr. Chu and the Registrant is incorporated herein by reference from the Registrant's Annual Report on Form 10-K for the fiscal year ended February 28, 1998. Sale and Cancellation Letter Agreement, dated January 7, 2002, between the Registrant and Mr. Chu is incorporated herein by reference from the Registrant's quarterly report on Form 10-Q for the fiscal quarter ended December 1, 2001.

Edgar Filing: NAUTICA ENTERPRISES INC - Form 10-Q

10(iii)(g) Employment Agreement, dated October 1, 1999, by and between the Registrant and John Varvatos, and Split Dollar Agreement, dated May 5, 2000, by and between the Registrant and John Varvatos are incorporated herein by reference from the Registrant's Annual Report on Form 10-K for the fiscal year ended March 4, 2000.

(b) Reports on Form 8-K. None

- 18 -

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.

NAUTICA ENTERPRISES, INC.

By: s/ Harvey Sanders

Harvey Sanders
Chairman of the Board
and President

Date: July 16, 2002

By: s/ Wayne A. Marino

Wayne A. Marino
Chief Financial Officer

Date: July 16, 2002

- 19 -