

G&K SERVICES INC  
Form 10-Q  
February 01, 2008

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**  
**FORM 10-Q**  
**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)**  
**OF THE SECURITIES EXCHANGE ACT OF 1934**  
**For the quarterly period ended December 29, 2007**  
**Commission file number 0-4063**  
**G&K SERVICES, INC.**  
(Exact name of registrant as specified in its charter)

MINNESOTA

41-0449530

(State or other jurisdiction of  
incorporation or organization)

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

5995 OPUS PARKWAY  
MINNETONKA, MINNESOTA 55343

(Address of principal executive offices and zip code)

Registrant's telephone number, including area code (952) 912-5500

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 non-accelerated filer. See definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 of the Exchange Act (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date.

Common Stock, par value \$0.50 per share, outstanding  
January 28, 2008 was 19,945,594 shares

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**PART I**  
**FINANCIAL INFORMATION**

**ITEM 1. FINANCIAL STATEMENTS**  
**CONSOLIDATED CONDENSED BALANCE SHEETS**

*G&K Services, Inc. and Subsidiaries*

|  | December 29,<br>2007<br>(Unaudited) | June 30,<br>2007 |
|--|-------------------------------------|------------------|
| (In thousands)   |                                     |                  |
| <b>ASSETS</b>  |                                     |                  |
| <b>Current Assets</b>  |                                     |                  |
| Cash and cash equivalents  | \$ 14,953                           | \$ 22,759        |
| Accounts receivable, less allowance for doubtful accounts of \$3,766 and \$3,405 | 113,465                             | 98,276           |
| Inventories, net   | 142,161                             | 140,780          |
| Prepaid expenses   | 14,880                              | 14,912           |
| Total current assets   | 285,459                             | 276,727          |
| <b>Property, Plant and Equipment, net</b>  | 255,700                             | 255,996          |
| <b>Goodwill, net</b>   | 421,674                             | 380,070          |
| <b>Other Assets</b>  | 78,080                              | 79,021           |
|  | \$ 1,040,913                        | \$ 991,814       |
| <b>LIABILITIES AND STOCKHOLDERS EQUITY</b>                                       |                                     |                  |
| <b>Current Liabilities</b>   |                                     |                  |
| Accounts payable   | \$ 25,521                           | \$ 21,911        |
| Accrued expenses   | 73,698                              | 68,927           |
| Deferred income taxes  | 6,913                               | 6,568            |
| Current maturities of long-term debt   | 7,864                               | 65,838           |
| Total current liabilities  | 113,996                             | 163,244          |
| <b>Long-Term Debt, net of Current Maturities</b>                                 | 256,859                             | 149,005          |
| <b>Deferred Income Taxes</b>   | 27,393                              | 34,298           |
| <b>Accrued Income Taxes Long Term</b>  | 11,349                              |                  |
| <b>Other Noncurrent Liabilities</b>  | 47,867                              | 53,279           |
| <b>Stockholders Equity</b>   | 583,449                             | 591,988          |
|  | \$ 1,040,913                        | \$ 991,814       |

The accompanying notes are an integral part of these consolidated condensed financial statements.

**Table of Contents****CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS***G&K Services, Inc. and Subsidiaries*

(Unaudited)

|  | For the Three Months    |                         | For the Six Months Ended |                         |
|--|-------------------------|-------------------------|--------------------------|-------------------------|
|  | December<br>29,<br>2007 | December<br>30,<br>2006 | December<br>29,<br>2007  | December<br>30,<br>2006 |
| (In thousands, except per share data)                    |                         |                         |                          |                         |
| <b>Revenues</b>  |                         |                         |                          |                         |
| Rental operations  | \$ 232,208              | \$ 209,130              | \$ 458,276               | \$ 416,431              |
| Direct sales   | 23,060                  | 21,634                  | 40,778                   | 37,461                  |
| Total revenues   | 255,268                 | 230,764                 | 499,054                  | 453,892                 |
| <b>Operating Expenses</b>                                |                         |                         |                          |                         |
| Cost of rental operations*                               | 148,071                 | 134,833                 | 291,057                  | 266,485                 |
| Cost of direct sales*                                    | 16,492                  | 15,617                  | 29,226                   | 27,656                  |
| Selling and administrative                               | 54,588                  | 50,042                  | 106,789                  | 99,921                  |
| Depreciation and amortization                            | 12,385                  | 11,232                  | 24,414                   | 22,450                  |
| Total operating expenses                                 | 231,536                 | 211,724                 | 451,486                  | 416,512                 |
| <b>Income from Operations</b>                            | 23,732                  | 19,040                  | 47,568                   | 37,380                  |
| Interest expense   | 3,990                   | 3,486                   | 7,948                    | 6,879                   |
| <b>Income before Income Taxes</b>                        | 19,742                  | 15,554                  | 39,620                   | 30,501                  |
| Provision for income taxes                               | 7,305                   | 5,910                   | 14,819                   | 11,665                  |
| <b>Net Income</b>  | \$ 12,437               | \$ 9,644                | \$ 24,801                | \$ 18,836               |
| Basic weighted average number of shares<br>outstanding   | 20,627                  | 21,190                  | 20,868                   | 21,187                  |
| <b>Basic Earnings per Common Share</b>                   | \$ 0.60                 | \$ 0.46                 | \$ 1.19                  | \$ 0.89                 |
| Diluted weighted average number of shares<br>outstanding | 20,783                  | 21,385                  | 21,054                   | 21,374                  |
| <b>Diluted Earnings per Common Share</b>                 | \$ 0.60                 | \$ 0.45                 | \$ 1.18                  | \$ 0.88                 |
| <b>Dividends per share</b>                               | \$ 0.05                 | \$ 0.04                 | \$ 0.10                  | \$ 0.08                 |

\* Excludes  
depreciation and  
intangible  
amortization

The accompanying notes are an integral part of these consolidated condensed financial statements.



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(Unaudited)

|  | For the Six Months Ended |                |
|--|--------------------------|----------------|
|  | December                 | December       |
|  | 29,                      | 30,            |
| (In thousands)   | 2007                     | 2006           |
| <b>Operating Activities:</b>   |                          |                |
| Net income   | \$ 24,801                | \$ 18,836      |
| Adjustments to reconcile net income to net cash provided by operating activities |                          |                |
| -  |                          |                |
| Depreciation and amortization  | 24,414                   | 22,450         |
| Other Adjustments  | 282                      | 1,732          |
| Changes in current operating items, exclusive of acquisitions                    | (9,290)                  | (16,260)       |
| Other assets and liabilities   | 3,286                    | 1,276          |
| Net cash provided by operating activities  | 43,493                   | 28,034         |
| <b>Investing Activities:</b>   |                          |                |
| Property, plant and equipment additions, net                                     | (8,525)                  | (18,355)       |
| Acquisitions of business assets, net   | (45,204)                 | 50             |
| Purchase of investments, net   | (1,887)                  | (1,393)        |
| Net cash used for investing activities   | (55,616)                 | (19,698)       |
| <b>Financing Activities:</b>   |                          |                |
| Repayments of long-term debt   | (7,133)                  | (7,440)        |
| Proceeds from (repayments of) short-term borrowings, net                         | 57,001                   | (7,759)        |
| Cash dividends paid  | (2,100)                  | (857)          |
| Sale of common stock   | 3,289                    | 2,743          |
| Repurchase of common stock shares  | (47,227)                 |                |
| Net cash provided by (used for) financing activities                             | 3,830                    | (13,313)       |
| <b>Decrease in Cash and Cash Equivalents</b>                                     | <b>(8,293)</b>           | <b>(4,977)</b> |
| <b>Effect of Exchange Rates on Cash</b>  | <b>487</b>               | <b>(681)</b>   |
| <b>Cash and Cash Equivalents:</b>  |                          |                |
| Beginning of period  | 22,759                   | 19,690         |
| End of period  | \$ 14,953                | \$ 14,032      |

The accompanying notes are an integral part of these consolidated condensed financial statements.

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G&K SERVICES, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS  
(Amounts in millions, except per share data)  
Three and six month periods ended December 29, 2007 and December 30, 2006  
(Unaudited)

**1. Basis of Presentation for Interim Financial Statements**

The consolidated condensed financial statements included herein, except for the June 30, 2007 balance sheet which was derived from the audited consolidated financial statements for the fiscal year ended June 30, 2007, have been prepared by us, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. In our opinion, the accompanying unaudited consolidated condensed financial statements contain all adjustments (consisting of only normal recurring adjustments) necessary to present fairly our financial position as of December 29, 2007, and the results of our operations for the three and six months ended and our cash flows for the six months ended December 29, 2007 and December 30, 2006. Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although we believe that the disclosures herein are adequate to make the information presented not misleading. It is suggested that these consolidated condensed financial statements be read in conjunction with the consolidated financial statements and the notes thereto included in our latest report on Form 10-K.

The accounting policies we follow are set forth in Note 1 in our Annual Report on Form 10-K for the fiscal year ended June 30, 2007.

The results of operations for the three and six month periods ended December 29, 2007 and December 30, 2006 are not necessarily indicative of the results to be expected for the full year.

**2. Adoption of New Accounting Pronouncements**

On July 13, 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes – an Interpretation of FASB Statement No. 109, which fundamentally changes the way that we are required to account for our uncertain tax positions for financial accounting purposes and is effective for our fiscal year beginning July 1, 2007. FIN 48 prescribes rules regarding how we should recognize, measure and disclose in our financial statements the tax positions that we have taken or will take on our tax return that are reflected in measuring current or deferred income tax assets and liabilities for interim or annual periods. Differences between tax positions taken in a tax return and amounts recognized in the financial statements will generally result in an increase in a liability for income taxes payable, or a reduction in a deferred tax asset or an increase in a deferred tax liability.

As a result of the implementation of FIN 48, we recognized a \$1.6 million decrease to the beginning balance of retained earnings on our balance sheet. At the adoption date of July 1, 2007, we had \$13.7 million of unrecognized tax benefits, of which \$4.2 million would favorably affect our effective tax rate in any future periods, if recognized.

We or one or more of our subsidiaries file income tax returns in the U.S., Canada and multiple state jurisdictions. We have substantially concluded on all U.S. Federal and Canadian income tax examinations through fiscal years 2004 and 2003, respectively. With few exceptions, we are no longer subject to state and local income tax examinations for years before fiscal year 2003.



We continue to recognize interest and penalties related to uncertain tax positions as a component of income tax expense. Upon adoption of FIN 48, we had \$1.8 million of accrued interest and penalties related to uncertain tax positions, of which \$1.4 million would favorably affect our effective tax rate in any future periods, if recognized.

We are not aware of any tax positions for which it is reasonably possible that the total amounts of unrecognized tax benefits will significantly change in the next 12 months.

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In September 2006, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 157, Fair Value Measurement (SFAS 157). SFAS 157 provides a definition of fair value, provides guidance for measuring fair value in U.S. GAAP and expands disclosures about fair value measurement. SFAS 157 will be effective at the beginning of fiscal 2009.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS 159). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS 159 will be effective at the beginning of fiscal 2009.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141 (revised 2007), Business Combinations (SFAS 141(R)). SFAS 141(R) will change how business acquisitions are accounted for and will impact financial statements both on the acquisition date and in subsequent periods. SFAS 141(R) will be effective at the beginning of fiscal 2010.

We are currently evaluating the impact of SFAS 157, SFAS 159 and SFAS 141(R) on our consolidated financial statements.

**3. Per Share Data**

Basic earnings per common share was computed by dividing net income by the weighted average number of shares of common stock outstanding during the period. Diluted earnings per common share was computed similarly to the computation of basic earnings per share, except that the denominator is increased for the assumed exercise of dilutive options and other dilutive securities, including non-vested restricted stock, using the treasury stock method.

|  | Three Months Ended      |                         | Six Months Ended        |                         |
|--|-------------------------|-------------------------|-------------------------|-------------------------|
|  | December<br>29,<br>2007 | December<br>30,<br>2006 | December<br>29,<br>2007 | December<br>30,<br>2006 |
| Weighted average number of common shares outstanding used in computation of basic earnings per share | 20.6                    | 21.2                    | 20.9                    | 21.2                    |
| Weighted average effect of non-vested restricted stock grants and assumed exercise of options        | 0.2                     | 0.2                     | 0.2                     | 0.2                     |
| Shares used in computation of diluted earnings per share   | 20.8                    | 21.4                    | 21.1                    | 21.4                    |

Potential common shares related to our outstanding stock options and restricted stock grants of 1.0 million and 0.5 million for the three months ended December 29, 2007 and December 30, 2006, respectively, and 0.7 million and 0.5 million for the six months ended December 29, 2007 and December 30, 2006, respectively, were excluded from the computation of diluted earnings per share. Inclusion of these shares would have been anti-dilutive as the exercise price of these shares exceeded their market value.



**Table of Contents****4. Comprehensive Income**

For the three and six month periods ended December 29, 2007 and December 30, 2006, the components of comprehensive income were as follows:

|   | Three Months Ended      |                         | Six Months Ended        |                         |
|---|-------------------------|-------------------------|-------------------------|-------------------------|
|   | December<br>29,<br>2007 | December<br>30,<br>2006 | December<br>29,<br>2007 | December<br>30,<br>2006 |
| Net income  | \$ 12.4                 | \$ 9.6                  | \$ 24.8                 | \$ 18.8                 |
| Other comprehensive income:   |                         |                         |                         |                         |
| Foreign currency translation adjustments, net of tax                        | 2.6                     | (6.7)                   | 12.6                    | (6.7)                   |
| Net unrealized holding loss on derivative financial instruments, net of tax | (0.8)                   | (0.3)                   | (2.0)                   | (1.5)                   |
| Comprehensive income  | \$ 14.2                 | \$ 2.6                  | \$ 35.4                 | \$ 10.6                 |

**5. Inventories**

The components of inventory as of December 29, 2007 and June 30, 2007 are as follows:

|                        | December<br>29,<br>2007 | June 30,<br>2007 |
|------------------------|-------------------------|------------------|
| Raw Materials          | \$ 6.2                  | \$ 5.5           |
| Work in Process        | 3.5                     | 4.4              |
| Finished Goods         | 51.0                    | 52.9             |
| New Goods              | \$ 60.7                 | \$ 62.8          |
| Merchandise In Service | \$ 81.5                 | \$ 78.0          |
| Total Inventories      | \$ 142.2                | \$ 140.8         |

**6. Goodwill and Intangible Assets**

Goodwill includes the following:

|  | United<br>States | Canada  | Total    |
|--|------------------|---------|----------|
| Balance as of June 30, 2007                          | \$ 315.8         | \$ 64.3 | \$ 380.1 |
| Acquisitions, net of purchase accounting adjustments | 36.3             |         | 36.3     |
| Currency exchange and other                          |                  | 5.3     | 5.3      |
| Balance as of December 29, 2007                      | \$ 352.1         | \$ 69.6 | \$ 421.7 |

The net increase in goodwill includes an increase of approximately \$36.3 million related to two acquisitions in fiscal 2008 and an increase of approximately \$5.3 million resulting from a change in foreign currency exchange rates.

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Our other intangible assets, which are included in other assets on the consolidated condensed balance sheet, are as follows:

|                            | December<br>29,<br>2007 | June 30,<br>2007 |
|----------------------------|-------------------------|------------------|
| Other Intangible Assets:   |                         |                  |
| Customer Contracts         | \$ 117.6                | \$ 111.7         |
| Accumulated Amortization   | (74.6)                  | (68.5)           |
| Net                        | \$ 43.0                 | \$ 43.2          |
| Non-Competition Agreements | \$ 11.1                 | \$ 11.1          |
| Accumulated Amortization   | (9.8)                   | (9.4)            |
| Net                        | \$ 1.3                  | \$ 1.7           |

The customer contracts include the combined value of the written service agreements and the related customer relationship. We have determined that there are no customer relationships with a significant separate value. Amortization expense was \$5.6 million and \$5.4 million for the six months ended December 29, 2007 and December 30, 2006, respectively. Estimated amortization expense for each of the next five fiscal years based on the intangible assets as of December 29, 2007 is as follows:

|                |       |
|----------------|-------|
| 2008 remaining | \$5.4 |
| 2009           | 7.4   |
| 2010           | 7.2   |
| 2011           | 6.5   |
| 2012           | 5.7   |
| 2013           | 4.2   |

**7. Long-Term Debt**

We maintain a \$325.0 million unsecured revolving credit facility which expires in August 2010. As of December 29, 2007, borrowings outstanding under the revolving credit facility were \$106.5 million. The unused portion of the revolver may be used for general corporate purposes, acquisitions, share repurchases, working capital needs and to provide up to \$50.0 million in letters of credit. As of December 29, 2007, letters of credit outstanding against the revolver were \$21.0 million.

Borrowings under the revolving credit facility bear interest at 0.55% to 1.50% over the London Interbank Offered Rate ( LIBOR ), or the Canadian prime rate for Canadian borrowings, based on a leverage ratio calculated on a quarterly basis. Advances outstanding as of December 29, 2007 bear interest at a rate of 5.52%. We also pay a fee on the unused daily balance of the revolving credit facility based on a leverage ratio calculated on a quarterly basis.

We have issued \$50.0 million of 8.4% unsecured fixed rate private placement notes with certain institutional investors. The 10-year notes have an eight-year average life with a final maturity on July 20, 2010. Beginning on July 20, 2004, and annually thereafter to maturity, we will repay \$7.1 million of the principal amount at par. As of December 29, 2007, the outstanding balance was \$21.4 million.

We maintain a loan agreement whereby the lender will make loans to us on a revolving basis up to \$60.0 million. This agreement has a termination date of October 21, 2010. We are required to pay interest on outstanding loan balances at a rate per annum of one month LIBOR plus a margin or, if the lender is funding the loan through the issuance of commercial paper to third parties, at a rate per annum equal to a margin plus the average annual interest rate for such commercial paper. In connection with the loan agreement, we granted a first priority security interest in certain of our U.S. based receivables. The amount of funds available under the loan agreement will be based on the

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amount of eligible receivables less various reserve requirements. We used the net proceeds of this loan to reduce indebtedness under our unsecured credit facilities. At December 29, 2007, there was \$60.0 million outstanding under the agreement at a current interest rate of 4.78%.

We have \$75.0 million of unsecured variable rate private placement notes. The notes bear interest at 0.60% over LIBOR and are scheduled to mature on June 30, 2015. The notes do not require principal payments until maturity. The interest rate and interest payments are reset and paid on a quarterly basis. As of December 29, 2007, the outstanding balance of the notes was \$75.0 million at a current rate of 5.46%.

**8. Share-Based Compensation**

We grant share-based awards, including restricted stock and options to purchase our common stock. Stock option grants are for a fixed number of shares to employees and directors with an exercise price equal to the fair value of the shares at the date of grant. Share-based compensation for awards is recognized in the consolidated statements of operations on a straight-line basis over the requisite service period. The amortization of share-based compensation reflects estimated forfeitures adjusted for actual forfeiture experiences. Our estimated forfeiture rate is reviewed and updated on an annual basis. As share-based compensation expense is recognized, a deferred tax asset is recorded that represents an estimate of the future tax deduction from the exercise of stock options or release of restrictions on the restricted stock. At the time share-based awards are exercised, cancelled, expire or restrictions lapse, we recognize adjustments to income tax expense. Total compensation expense related to share-based awards was \$1.5 million and \$1.1 million for the three months ended and \$2.6 million and \$2.1 million for the six months ended December 29, 2007 and December 30, 2006. The number of options that have been exercised and restricted stock that vested since June 30, 2007, was 0.1 million shares.

**9. Employee Benefit Plans**

Effective January 1, 2007, we froze our pension and Supplemental Executive Retirement Plan (SERP). As a result, there has been no future growth in benefits since December 31, 2006. As noted below, net periodic pension cost has been significantly reduced.

The components of net periodic pension cost are as follows for the three months ended December 29, 2007 and December 30, 2006:

|                           | Pension Plan       |                   | Supplemental Executive Retirement Plan |                   |
|---------------------------|--------------------|-------------------|--|-------------------|
|                           | Three Months Ended |                   | Three Months Ended                     |                   |
|                           | December 29, 2007  | December 30, 2006 | December 29, 2007                      | December 30, 2006 |
| Service cost              | \$                 | \$ 0.7            | \$                                     | \$ 0.1            |
| Interest cost             | 0.8                | 0.8               | 0.2                                    | 0.2               |
| Expected return on assets | (1.1)              | (0.7)             |  |                   |
| Net periodic pension cost | \$ (0.3)           | \$ 0.8            | \$ 0.2                                 | \$ 0.3            |

The components of net periodic pension cost are as follows for the six months ended December 29, 2007 and December 30, 2006:

|  | Pension Plan | Supplemental Executive Retirement Plan |
|--|--------------|--|
|--|--------------|--|



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|                           | Six Months Ended        |                         | Six Months Ended        |                         |
|---------------------------|-------------------------|-------------------------|-------------------------|-------------------------|
|                           | December<br>29,<br>2007 | December<br>30,<br>2006 | December<br>29,<br>2007 | December<br>30,<br>2006 |
| Service cost              | \$                      | \$ 1.4                  | \$                      | \$ 0.3                  |
| Interest cost             | 1.6                     | 1.6                     | 0.4                     | 0.4                     |
| Expected return on assets | (1.8)                   | (1.4)                   |                         |                         |
| Net periodic pension cost | \$ (0.2)                | \$ 1.6                  | \$ 0.4                  | \$ 0.7                  |

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We have two operating segments, United States and Canada, which have been identified as components of our Company that are reviewed by our Chief Executive Officer to determine resource allocation and evaluate performance. Each operating segment derives revenues from the branded identity apparel and facility services industry, which includes garment rental and non-apparel items such as floor mats, dust mops, wiping towels, selected linen items and restroom products. No single customer accounted for more than 1.5% of our consolidated revenue.

Corporate expenses are allocated to the segments based on segment revenue. We evaluate performance based on income from operations. Financial information by geographic location for the three and six month periods ended December 29, 2007 and December 30, 2006 is as follows:

| For the Three Months Ended            | United States | Canada  | Total    |
|---------------------------------------|---------------|---------|----------|
| Second Quarter Fiscal Year 2008:      |               |         |          |
| Revenues                              | \$ 208.3      | \$ 47.0 | \$ 255.3 |
| Income from operations                | 15.9          | 7.8     | 23.7     |
| Depreciation and amortization expense | 10.6          | 1.8     | 12.4     |
| Second Quarter Fiscal Year 2007:      |               |         |          |
| Revenues                              | \$ 191.1      | \$ 39.7 | \$ 230.8 |
| Income from operations                | 12.5          | 6.5     | 19.0     |
| Depreciation and amortization expense | 9.6           | 1.6     | 11.2     |
|                                       |               |         |          |
| For the Six Months Ended              | United States | Canada  | Total    |
| Fiscal Year 2008:                     |               |         |          |
| Revenues                              | \$ 408.6      | \$ 90.5 | \$ 499.1 |
| Income from operations                | 30.4          | 17.2    | 47.6     |
| Depreciation and amortization expense | 20.8          | 3.6     | 24.4     |
| Fiscal Year 2007:                     |               |         |          |
| Revenues                              | \$ 374.4      | \$ 79.5 | \$ 453.9 |
| Income from operations                | 24.5          | 12.9    | 37.4     |
| Depreciation and amortization expense | 19.2          | 3.3     | 22.5     |

For the three months ended December 29, 2007, the Canada segment results were negatively impacted by \$0.9 million, resulting from a fire at a production facility. These expenses included our insurance deductible, estimated unrecoverable extra expenses incurred and a partial impairment of our customer intangible assets. For the six months ended December 29, 2007, the Canada segment results were positively impacted by \$0.7 million, resulting from the net effect of a gain on the sale of property, offset by fire expenses. The net Canadian impact was offset by expenses in our United States segment during the six months ended December 29, 2007, which included severance associated with the restructuring of our manufacturing operations and certain management positions, an increase in our inventory reserves and expenses associated with certain legal matters all of which occurred in the first quarter of fiscal 2008. The net effect of these items on the United States segment was approximately \$1.7 million of expense for the six months ended December 29, 2007.



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

(Unaudited)

**Overview**

G&K Services, Inc., founded in 1902 and currently headquartered in Minnetonka, Minnesota, is a market leader in providing branded identity apparel and facility services programs that enhance image and safety in the workplace. We serve a wide variety of North American industrial, service and high-technology companies providing them with rented uniforms and facility services products such as floor mats, dust mops, wiping towels, restroom supplies and selected linen items. We also sell uniforms and other apparel items to customers in our direct sale programs. The North American rental market is approximately \$7.0 billion, while the portion of the direct sale market targeted by us is approximately \$5.0 billion.

Our industry continues to consolidate from many family owned and small local providers to several large providers. We are participating in this industry consolidation. Our rental acquisition strategy is focused on acquisitions in the rental and direct purchase businesses that expand our geographic presence and/or expand our local market share in order to further leverage our existing production facilities.

In the second quarter of fiscal year 2008, our revenue was \$255.3 million, a 10.6% increase from the \$230.8 million reported during the second quarter of fiscal 2007. Continued momentum in rental organic growth throughout 2007 and into 2008, along with acquisitions and the strengthening Canadian dollar, drove the increase compared to the prior year.

Earnings per diluted share was \$0.60 for the quarter compared to \$0.45 during the prior-year quarter. These results reflect leveraging the increased revenue in the second quarter of fiscal year 2008, implementation of improved pricing controls during fiscal 2007 and productivity improvements from our handheld and other initiatives.

In July 2007, we acquired the outstanding stock and certain real estate from Leef Brothers, Inc. (Leef Services), a uniform and facility services company serving customers in the Upper Midwest. This acquisition strengthens our market position and increases the utilization of our existing operations. The proforma effect of this acquisition, had it been acquired at the beginning of each fiscal year, was not material.

**Critical Accounting Policies**

The discussion of the financial condition and results of operations are based upon the consolidated condensed financial statements, which have been prepared in conformity with United States generally accepted accounting principles. As such, management is required to make certain estimates, judgments and assumptions that are believed to be reasonable based on the information available. These estimates and assumptions affect the reported amount of assets and liabilities, revenues and expenses, and disclosure of contingent assets and liabilities at the date of the financial statements. Actual results may differ from these estimates under different assumptions or conditions.

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, the most important and pervasive accounting policies used and areas most sensitive to material changes from external factors. See Note 1 to the consolidated condensed financial statements in our Annual Report on Form 10-K for the fiscal year ended June 30, 2007 for additional discussion of the application of these and other accounting policies.

**Table of Contents****Results of Operations**

The percentage relationships to revenues of certain income and expense items for the three and six month periods ended December 29, 2007 and December 30, 2006, and the percentage changes in these income and expense items between periods are presented in the following table:

|                                  | Three Months Ended |                   | Six Months Ended  |                   | Percentage Change                         |   |
|----------------------------------|--------------------|-------------------|-------------------|-------------------|---|---|
|                                  | December 29, 2007  | December 30, 2006 | December 29, 2007 | December 30, 2006 | Three Months<br>FY 2008<br>vs. FY<br>2007 | Six Months<br>FY 2008<br>vs. FY<br>2007 |
|                                  | Revenues:          |                   |                   |                   |   |   |
| Rental                           | 91.0%              | 90.6%             | 91.8%             | 91.7%             | 11.0%                                     | 10.0%                                   |
| Direct                           | 9.0                | 9.4               | 8.2               | 8.3               | 6.6                                       | 8.9                                     |
| Total revenues                   | 100.0              | 100.0             | 100.0             | 100.0             | 10.6                                      | 9.9                                     |
| Expenses:                        |                    |                   |                   |                   |   |   |
| Cost of rental sales             | 63.8               | 64.5              | 63.5              | 64.0              | 9.8                                       | 9.2                                     |
| Cost of direct sales             | 71.5               | 72.2              | 71.7              | 73.8              | 5.6                                       | 5.7                                     |
| Total cost of sales              | 64.5               | 65.2              | 64.2              | 64.8              | 9.4                                       | 8.9                                     |
| Selling and administrative       | 21.4               | 21.7              | 21.4              | 22.0              | 9.1                                       | 6.9                                     |
| Depreciation and<br>amortization | 4.8                | 4.8               | 4.9               | 5.0               | 10.3                                      | 8.7                                     |
| Income from operations           | 9.3                | 8.3               | 9.5               | 8.2               | 24.6                                      | 27.3                                    |
| Interest expense                 | 1.6                | 1.6               | 1.6               | 1.5               | 14.5                                      | 15.5                                    |
| Income before income<br>taxes    | 7.7                | 6.7               | 7.9               | 6.7               | 26.9                                      | 29.9                                    |
| Provision for income<br>taxes    | 2.8                | 2.5               | 2.9               | 2.6               | 23.6                                      | 27.0                                    |
| Net income                       | 4.9%               | 4.2%              | 5.0%              | 4.1%              | 29.0%                                     | 31.7%                                   |

**Three months ended December 29, 2007 compared to three months ended December 30, 2006**

**Revenues.** Total revenue in the second quarter of fiscal 2008 increased 10.6% to \$255.3 million from \$230.8 million in the second quarter of fiscal 2007. Rental revenue increased \$23.1 million, or 11.0% in the second quarter. Our organic rental growth rate was approximately 3.75% in the quarter. Organic rental growth was driven by strong new account sales, record quarterly route sales and improved pricing controls. These strong results were offset by softness in the overall economy, which has resulted in a net reduction in the number of employees wearing uniforms and a reduction in ancillary products rented by existing customers. In addition, the increase in rental revenue was aided by

the strong Canadian dollar and the recent acquisitions of Alltex, Grantex and Leef Services. The organic rental growth rate is calculated using rental revenue, adjusted for foreign currency exchange rate changes and revenue from newly acquired businesses compared to prior-period results. We believe that the organic rental growth rate better reflects the growth of our existing rental business and is therefore useful in analyzing our financial condition and results of operations.

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Direct sale revenue increased 6.6% to \$23.1 million in the second quarter of fiscal 2008 compared to \$21.6 million in the same period of fiscal 2007. The organic direct sale growth rate during the current period was approximately 3.0%. *Cost of Rental.* Cost of rental operations increased 9.8% to \$148.1 million in the second quarter of fiscal 2008 from \$134.8 million in the same period of fiscal 2007. As a percentage of rental revenue, our gross margin from rental sales increased to 36.2% in the second quarter of fiscal 2008 from 35.5% in the same period of fiscal 2007. The improvement in rental gross margin resulted primarily from improved leverage from overall rental revenue growth, including lower merchandise and production costs. Production cost savings were driven in part by continued execution of ongoing productivity initiatives. These improvements in rental gross margin were partially offset by increased delivery costs due to higher energy prices.

*Cost of Direct Sales.* Cost of direct sales increased 5.6% to \$16.5 million in the second quarter of fiscal 2008 from \$15.6 million in the same period of fiscal 2007. Gross margin from direct sales improved to 28.5% in the second quarter of fiscal 2008 from 27.8% in the second quarter of fiscal 2007. The improvement in gross margin was primarily due to pricing and improved efficiencies from higher volume.

*Selling and Administrative.* Selling and administrative expenses increased 9.1% to \$54.6 million in the second quarter of fiscal 2008 from \$50.0 million in the same period of fiscal 2007. As a percentage of total revenues, selling and administrative expenses decreased to 21.4% in the second quarter of fiscal 2008 from 21.7% in the second quarter of fiscal 2007. The improvement in selling and administrative expenses as a percent of revenue is the result of leveraging our existing infrastructure to support increased revenues and administrative efficiencies gained from our handheld technology platform. This improvement was partially offset by costs associated with a fire at a production facility, which included our insurance deductible, extra costs not covered by insurance and an impairment charge related to certain customer intangibles.

*Depreciation and Amortization.* Depreciation and amortization expense increased 10.3% to \$12.4 million in the second quarter of fiscal 2008 from \$11.2 million in the same period of fiscal 2007. This increase was due to the increased depreciation expense from acquired businesses partially offset by lower capital expenditures. As a percentage of total revenues, depreciation and amortization expense remained at 4.8% for the second quarter of both fiscal years.

*Interest Expense.* Interest expense was \$4.0 million in the second quarter of fiscal 2008, up from \$3.5 million in the same period of fiscal 2007. The increase was primarily due to higher debt levels resulting from our share repurchase program and acquisitions as well as increased average interest rates.

*Provision for Income Taxes.* Our effective tax rate decreased to 37.0% in the second quarter of fiscal 2008 from 38.0% in the same period of fiscal 2007. The decrease in the tax rate was primarily due to the enactment of a federal tax rate reduction in Canada during the three months ended December 29, 2007.

***Six months ended December 29, 2007 compared to six months ended December 30, 2006***

*Revenues.* Total revenue for the first six months of fiscal 2008 increased 9.9% to \$499.1 million from \$453.9 million for the same period of fiscal 2007. Rental revenue increased \$41.8 million, or 10.0% in the first six months. Our organic rental growth rate was approximately 3.5% in 2008 versus 4.75% in 2007. Organic rental growth resulted from increased route sales, new account sales and improved pricing controls, offset by softness in the overall economy, which has resulted in a net reduction in the number of employees wearing uniforms and a reduction in ancillary products rented by existing customers. In addition, rental revenue increased due to the impact of the strong Canadian dollar and our recent acquisitions. Direct sale revenue increased 8.9% to \$40.8 million in the first six months of fiscal 2008 compared to \$37.5 million in the same period of fiscal 2007. The organic direct sale growth rate during the current period was approximately 5.5%. The increase in direct sale revenue is largely due to organic growth during the period.

*Cost of Rental and Direct Sale.* Cost of rental operations increased 9.2% to \$291.1 million in the first six months of fiscal 2008 from \$266.5 million in the same period of fiscal 2007. Gross margin from rental sales improved to 36.5% in the first six months of fiscal 2008 from 36.0% in the same period of fiscal 2007. The improvement in rental margins is the primarily the result of leveraging our overall rental growth and lower merchandise and production costs. As noted previously, production cost savings were driven in part by continued execution of ongoing productivity initiatives. Cost of direct sales increased 5.7% to \$29.2 million in the first six months of fiscal 2008 from

\$27.7 million in the same period of fiscal 2007. Gross margin from direct sales improved to 28.3% in the first six months of fiscal 2008 from 26.2% in the same period of fiscal 2007. The improvement in direct sales margins is the result of cost savings measures as well as improved pricing.



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*Selling and Administrative.* Selling and administrative expenses increased 6.9% to \$106.8 million in the first six months of fiscal 2008 from \$99.9 million in the same period of fiscal 2007. As a percentage of total revenues, selling and administrative expenses decreased to 21.4% in the first six months of fiscal 2008 from 22.0% in the same period of fiscal 2007. Selling and administrative expenses decreased as a percent of revenue due to the leveraging of our existing infrastructure to support higher sales volume and the efficiencies gained through the rollout of our handheld technology throughout our route delivery organization and other productivity initiatives. As previously noted, these improvements were partially offset by costs associated with a fire at a production facility.

*Depreciation and Amortization.* Depreciation and amortization expense increased 8.7% to \$24.4 million in the first six months of fiscal 2008 from \$22.5 million in the same period of fiscal 2007. The increase was due to depreciation and amortization associated with acquired businesses partially offset by lower capital expenditures. As a percentage of total revenues, depreciation and amortization expense decreased to 4.9% in the first six months of fiscal 2008 from 5.0% in the same period of fiscal 2007.

*Interest Expense.* Interest expense was \$7.9 million in the first six months of fiscal 2008, up from \$6.9 million in the same period of fiscal 2007. The increase was primarily due to increased debt levels resulting from our share repurchase program and recent acquisitions as well as higher average interest rates.

*Provision for Income Taxes.* Our effective tax rate decreased to 37.4% in the first six months of fiscal 2008 from 38.2% in the same period of fiscal 2007. The decrease in the tax rate was primarily due to the enactment of a federal tax rate reduction in Canada during the three months ended December 29, 2007.

***Liquidity, Capital Resources and Financial Condition***

Our primary sources of cash are net cash flows from operations and borrowings under our debt arrangements. Primary uses of cash are interest payments on indebtedness, capital expenditures, acquisitions, share repurchases and general corporate purposes.

Working capital at December 29, 2007 was \$171.5 million, up 51.1% from \$113.5 million at June 30, 2007. The increase in working capital is primarily due to the renewal of a credit facility which resulted in a reclassification of \$58.0 million to long term debt from current maturities in the first quarter of fiscal 2008.

*Operating Activities.* Net cash provided by operating activities was \$43.5 million in the first six months of fiscal 2008 and \$28.0 million in the same period of fiscal 2007. The increase in cash generated from operating activities is largely due to improved net income as well as lower payments on our accounts payables during the six months ended December 29, 2007.

*Investing Activities.* Net cash used in investing activities was \$55.6 million in the first six months of fiscal 2008 and \$19.7 million in the same period of fiscal 2007. In fiscal 2008, cash was used primarily for business acquisitions and purchases of property, plant and equipment. In fiscal 2007, cash was primarily used to purchase property, plant and equipment.

*Financing Activities.* Cash provided by financing activities was \$3.8 million in the first six months of fiscal 2008 and cash used for financing activities was \$13.3 million in the same period of fiscal 2007. Cash provided by financing activities in fiscal 2008 was principally from our credit facilities and the proceeds were partially offset by cash outlays for our share repurchase program. Cash used by financing activities in fiscal 2007 was principally for the repayment of short-term and long-term borrowings. The Company paid dividends of \$2.1 million during the first six months of fiscal 2008.

We maintain a \$325.0 million unsecured revolving credit facility which expires in August 2010. As of December 29, 2007, borrowings outstanding under the revolving credit facility were \$106.5 million. The unused portion of the revolver may be used for general corporate purposes, acquisitions, share repurchases, working capital needs and to provide up to \$50.0 million in letters of credit. As of December 29, 2007, letters of credit outstanding against the revolver were \$21.0 million.

Borrowings under the revolving credit facility bear interest at 0.55% to 1.50% over the London Interbank Offered Rate ( LIBOR ), or the Canadian prime rate for Canadian borrowings, based on a leverage ratio calculated on a quarterly basis. Advances outstanding as of December 29, 2007 bear interest at a rate of 5.52%. We also pay a fee on the unused daily balance of the revolving credit facility based on a leverage ratio calculated on a quarterly basis.



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We have issued \$50.0 million of 8.4% unsecured fixed rate private placement notes with certain institutional investors. The 10-year notes have an eight-year average life with a final maturity on July 20, 2010. Beginning on July 20, 2004, and annually thereafter to maturity, we will repay \$7.1 million of the principal amount at par. As of December 29, 2007, the outstanding balance was \$21.4 million.

We maintain a loan agreement whereby the lender will make loans to us on a revolving basis up to \$60.0 million. This agreement expires in October 2010. We are required to pay interest on outstanding loan balances at a rate per annum of one month LIBOR plus a margin or, if the lender is funding the loan through the issuance of commercial paper to third parties, at a rate per annum equal to a margin plus the average annual interest rate for such commercial paper. In connection with the loan agreement, we granted a first priority security interest in certain of our U.S. based receivables. The amount of funds available under the loan agreement will be based on the amount of eligible receivables less various reserve requirements. We used the net proceeds of this loan to reduce indebtedness under our unsecured credit facilities. At December 29, 2007, there was \$60.0 million outstanding under the agreement at a current interest rate of 4.78%.

We have \$75.0 million of unsecured variable rate private placement notes. The notes bear interest at 0.60% over LIBOR and are scheduled to mature on June 30, 2015. The notes do not require principal payments until maturity. The interest rate and interest payments are reset and paid on a quarterly basis. As of December 29, 2007, the outstanding balance of the notes was \$75.0 million at a current rate of 5.46%.

*Cash Obligations.* Under various agreements, we are obligated to make future cash payments in fixed amounts. These include payments under the variable rate term loan and revolving credit facility, the fixed rate term loan, capital lease obligations and rent payments required under non-cancelable operating leases with initial or remaining terms in excess of one year.

At December 29, 2007, we had available cash on hand of \$15.0 million and approximately \$197.5 million of available capacity under our revolving credit facility. We anticipate that we will generate sufficient cash flows from operations to satisfy our cash commitments and capital requirements for fiscal 2008 and to reduce the amounts outstanding under the revolving credit facility; however, we may utilize borrowings under the revolving credit facility to supplement our cash requirements from time to time. We estimate that capital expenditures in fiscal 2008 will be approximately \$25-\$27 million.

The amount of cash flow generated from operations could be affected by a number of risks and uncertainties. In fiscal 2008, we may actively seek and consider acquisitions of business assets. The consummation of any acquisition could affect our liquidity profile and level of outstanding debt. We believe that our earnings and cash flow from operations, existing credit facilities and our ability to obtain additional debt or equity capital, if necessary, will be adequate to finance acquisition opportunities.

***Off Balance Sheet Arrangements***

At December 29, 2007, we had \$21.0 million of stand-by letters of credit that were issued and outstanding, primarily in connection with our property and casualty insurance programs. No amounts have been drawn upon these letters of credit.

***Pension Obligations***

We account for our defined benefit pension plan using SFAS No. 87 *Employer's Accounting for Pensions* (SFAS 87) and SFAS No. 158 *Employer's Accounting for Defined Benefit Pension and Other Postretirement Plans*. Under SFAS 87, pension expense is recognized on an accrual basis over employees' approximate service periods. Pension expense calculated under SFAS 87 is generally independent of funding decisions or requirements. We recognized income of \$0.3 million for our defined benefit pension plan in the second quarter of fiscal 2008 and \$0.8 million of expense in the same period of fiscal 2007. At June 30, 2007, the fair value of our pension plan assets totaled \$41.5 million. Effective January 1, 2007 we have frozen our defined benefit pension plan and related supplemental executive retirement plan. We incurred \$0.2 million in costs associated with this action in fiscal year 2006. All benefits earned by defined benefit plan participants through the end of calendar year 2006 will be available upon retirement under plan provisions. Future growth in benefits did not occur beyond December 31, 2006.

The calculation of pension expense and the corresponding liability requires the use of a number of critical assumptions, including the expected long-term rate of return on plan assets and the assumed discount rate. Changes in

these assumptions can result in different expense and liability amounts, and future actual experience can differ from these assumptions. Pension expense increases as the expected rate of return on pension

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plan assets decreases. At June 30, 2007, we estimated that the pension plan assets will generate a long-term rate of return of 8.0%. This rate was developed by evaluating input from our outside actuary as well as long-term inflation assumptions. The expected long-term rate of return on plan assets at June 30, 2007 is based on an allocation of equity and fixed income securities. Decreasing the expected long-term rate of return by 0.5% (from 8.0% to 7.5%) would increase our estimated 2008 pension expense by approximately \$0.2 million. Pension liability and future pension expense increase as the discount rate is reduced. We discounted future pension obligations using a rate of 6.40% at June 30, 2007. Our outside actuary determines the discount rate by creating a yield curve based on high quality bonds. Decreasing the discount rate by 0.5% (from 6.40% to 5.90%) would increase our accumulated benefit obligation at June 30, 2007 by approximately \$4.9 million and would have an immaterial impact on our fiscal 2008 pension expense.

Future changes in plan asset returns, assumed discount rates and various other factors related to the participants in our pension plan will impact our future pension expense and liabilities. We cannot predict with certainty what these factors will be in the future.

***Litigation***

We are involved in a variety of legal actions relating to personal injury, employment, environmental and other legal matters that arise in the normal course of business. These legal actions include lawsuits that challenge the practice of charging for certain environmental services on invoices which were settled in the last fiscal year, and are presently being administered. None of these legal actions are expected to have a material adverse effect on our results of operations or financial position.

***Share-Based Compensation***

We grant share-based awards, including restricted stock and options to purchase our common stock. Stock option grants are for a fixed number of shares to employees and directors with an exercise price equal to the fair value of the shares at the date of grant. Share-based compensation for awards is recognized in the consolidated statements of operations on a straight-line basis over the requisite service period. The amortization of share-based compensation reflects estimated forfeitures adjusted for actual forfeiture experiences. Our estimated forfeiture rate is reviewed and updated on an annual basis. As share-based compensation expense is recognized, a deferred tax asset is recorded that represents an estimate of the future tax deduction from the exercise of stock options or release of restrictions on the restricted stock. At the time share-based awards are exercised, cancelled, expire or restrictions lapse, we recognize adjustments to income tax expense. Total compensation expense related to share-based awards was \$1.5 million and \$1.1 million for the three months ended and \$2.6 million and \$2.1 million for the six months ended December 29, 2007 and December 30, 2006. The number of options that have been exercised and restricted stock that vested since June 30, 2007, was 0.1 million shares.

***Adoption of New Accounting Pronouncements***

On July 13, 2006, the Financial Accounting Standards Board issued FASB Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes – an Interpretation of FASB Statement No. 109, which fundamentally changes the way that we are required to account for our uncertain tax positions for financial accounting purposes and is effective for our fiscal year beginning July 1, 2007. FIN 48 prescribes rules regarding how we should recognize, measure and disclose in our financial statements the tax positions that we have taken or will take on our tax return that are reflected in measuring current or deferred income tax assets and liabilities for interim or annual periods. Differences between tax positions taken in a tax return and amounts recognized in the financial statements will generally result in an increase in a liability for income taxes payable, or a reduction in a deferred tax asset or an increase in a deferred tax liability.

As a result of the implementation of FIN 48, we recognized a \$1.6 million decrease to the beginning balance of retained earnings on our balance sheet. At the adoption date of July 1, 2007, we had \$13.7 million of unrecognized tax benefits, of which \$4.2 million would favorably affect our effective tax rate in any future periods, if recognized.

We or one or more of our subsidiaries files income tax returns in the U.S., Canada and multiple state jurisdictions. We have substantially concluded on all U.S. federal and Canadian income tax examinations through fiscal years 2004 and 2003, respectively. With few exceptions, we are no longer subject to state and local income tax examinations for years before fiscal year 2003.



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We continue to recognize interest and penalties related to uncertain tax positions as a component of income tax expense. Upon adoption of FIN 48, we had \$1.8 million of accrued interest and penalties related to uncertain tax positions, of which \$1.4 million would favorably affect our effective tax rate in any future periods, if recognized. We are not aware of any tax positions for which it is reasonably possible that the total amounts of unrecognized tax benefits will significantly change in the next 12 months.

**Accounting Pronouncements Not Yet Adopted**

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, Fair Value Measurement (SFAS 157). SFAS 157 provides a definition of fair value, provides guidance for measuring fair value in U.S. GAAP and expands disclosures about fair value measurement. SFAS 157 will be effective at the beginning of fiscal 2009.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS 159). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS 159 will be effective at the beginning of fiscal 2009.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141 (revised 2007), Business Combinations (SFAS 141(R)). SFAS 141(R) will change how business acquisitions are accounted for and will impact financial statements both on the acquisition date and in subsequent periods. SFAS 141(R) will be effective at the beginning of fiscal 2010.

We are currently evaluating the impact of SFAS 157, SFAS 159 and SFAS 141(R) on our consolidated financial statements.

**Cautionary Statements Regarding Forward-Looking Statements**

The Private Securities Litigation Reform Act of 1995 provides a safe harbor from civil litigation for forward-looking statements. Forward-looking statements may be identified by words such as estimates, anticipates, projects, plans, expects, intends, believes, seeks, could, should, may and will or the negative versions thereof and similar and by the context in which they are used. Such statements are based upon our current expectations and speak only as of the date made. These statements are subject to various risks, uncertainties and other factors that could cause actual results to differ from those set forth in or implied by this quarterly report on Form 10-Q. Factors that might cause such a difference include, but are not limited to, the possibility of greater than anticipated operating costs, including energy costs, lower sales volumes, the performance and costs of integration of acquisitions or assumption of unknown liabilities in connection with acquisitions, fluctuations in costs of materials and labor, costs and possible effects of union organizing activities, loss of key management, uncertainties regarding any existing or newly-discovered expenses and liabilities related to environmental compliance and remediation, failure to achieve and maintain effective internal controls for financial reporting required by the Sarbanes-Oxley Act of 2002, the initiation or outcome of litigation, higher assumed sourcing or distribution costs of products, the disruption of operations from catastrophic events, changes in federal and state tax laws and the reactions of competitors in terms of price and service. We undertake no obligation to update any forward-looking statements to reflect events or circumstances arising after the date on which they are made except as required by law. Additional information concerning potential factors that could effect future financial results is included in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2007.

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**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK**

**Interest Rate Risk**

We are subject to market risk exposure related to changes in interest rates. We use financial instruments, including fixed and variable rate debt, as well as interest rate swaps to manage interest rate risk. Interest rate swap agreements are entered into for periods consistent with related underlying exposures and do not constitute positions independent of those exposures. Assuming the current level of borrowings, a one percentage point increase in interest rates under these borrowings would have increased our interest expense for the second quarter of fiscal 2008 by approximately \$0.4 million. This estimated exposure considers the mitigating effects of interest rate swap agreements outstanding at December 29, 2007 on the change in the cost of variable rate debt. The current fair market value of all outstanding contracts at December 29, 2007 is a negative \$2.6 million.

**Energy Cost Risk**

We use derivative financial instruments to manage the risk that changes in energy costs will have on our future financial results. We purchase futures contracts to effectively hedge a portion of anticipated energy purchases. The futures contracts are reflected at fair value in the consolidated balance sheet and the related gains or losses on these contracts are deferred in stockholders' equity (as a component of other comprehensive income) for contracts that cash flow hedge accounting is achieved or in the statements of operations depending on the effectiveness of the hedge. Upon settlement of each contract, the actual gain or loss is reflected in cost of rental operations. The current fair market value of all outstanding contracts at December 29, 2007 is a positive \$0.9 million.

**Foreign Currency Exchange Risk**

We have material foreign subsidiaries located in Canada. The assets and liabilities of these subsidiaries are denominated in the Canadian dollar and as such are translated into U.S. dollars at the exchange rate in effect at the balance sheet date. Results of operations are translated using the average exchange rates throughout the period. The effect of exchange rate fluctuations on translation of assets and liabilities are recorded as a component of stockholders' equity. Gains and losses from foreign currency transactions are included in results of operations.

**ITEM 4. CONTROLS AND PROCEDURES**

Under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, we conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rule 13a-15(e) or Rule 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended, as of the end of the period covered by this Form 10-Q. Based on their evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures are effective.

There have been no changes in our internal controls over financial reporting that occurred during the period covered by this Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.



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**PART II**  
**OTHER INFORMATION**

**ITEM 1A. RISK FACTORS**

In addition to the other information set forth in this Quarterly Report on Form 10-Q, you should carefully consider the factors discussed in Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended June 30, 2007, which could materially affect our business, financial condition or future results. There have been no material changes to the risk factors set forth in our Annual Report on Form 10-K for the year ended June 30, 2007. The risks described in our Annual Report on Form 10-K are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

The following table includes information about repurchases we made of our common stock during the periods indicated:

| Period  | Total<br>Number<br>of Shares<br>(or Units)<br>Purchased | Average<br>Price Paid<br>per Share<br>(or Unit) | Total Number<br>of<br>Shares (or<br>Units)<br>Purchased as<br>Part of<br>Publicly<br>Announced<br>Plans or<br>Programs | Maximum<br>Number<br><br>(or Approximate<br>Dollar Value) of<br>Shares (or Units)<br><br>that May Yet be<br>Purchased Under<br>the Plans or<br>Programs |
|---|---|---|--|---|
| <b>Month #1</b><br><b>(Fiscal month beginning September 30,</b><br><b>2007 and ending November 3, 2007)</b> | 186,700   | \$39.73   | 186,700  | \$ 73,447,243   |
| <b>Month #2</b><br><b>(Fiscal month beginning November 4,</b><br><b>2007 and ending December 1, 2007)</b>   | 299,078   | \$39.80   | 299,078  | \$ 61,534,484   |
| <b>Month #3</b><br><b>(Fiscal month beginning December 2,</b><br><b>2007 and ending December 29, 2007)</b>  | 427,407   | \$38.91   | 427,407  | \$ 44,889,770   |

In May 2007, our Board of Directors authorized the repurchase of up to \$100.0 million of G&K Services outstanding common stock. For the three months ended December 29, 2007, we purchased a total of 913,185 shares totaling \$36.0 million and for the six months ended December 29, 2007, we purchased 1,170,485 shares totaling \$46.2 million. Cash used for the purchase of shares totaled \$36.0 million for the three months ended and \$47.2 million for the six months ended December 29, 2007. The cash used during the six month period ending December 29, 2007 included \$1.0 million for shares repurchased in the fourth quarter of fiscal year 2007 but not paid until July 2, 2007. As of December 29, 2007, we had \$44.9 million remaining under this authorization.

**Table of Contents****ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

- a. The Company held its Annual Meeting of Shareholders on November 15, 2007.
- b. The following three persons were elected as directors: John S. Bronson, Wayne M. Fortun and Ernest J. Mrozek. The following six persons comprise the other directors whose terms of office continued after the Annual Meeting of Shareholders: Michael G. Allen, Paul Baszucki, J. Patrick Doyle, Richard L. Marcantonio, M. Lenny Pippin and Alice M. Richter.
- c. 1. Each director nominee received the following votes:

|             | <b>In Favor</b> | <b>Shares<br/>Withhold<br/>Authority</b> | <b>Broker<br/>Non-Votes</b> |
|-------------|-----------------|--|-----------------------------|
| Mr. Bronson | 19,223,250      | 255,769                                  | 0                           |
| Mr. Fortun  | 19,072,418      | 406,601                                  | 0                           |
| Mr. Mrozek  | 19,223,507      | 255,511                                  | 0                           |

2. Shareholders ratified the appointment of Ernst & Young LLP, Independent Registered Public Accounting Firm, as the Company's independent auditors for fiscal 2008: 19,265,180 shares in favor, 195,301 shares voting against and 18,535 shares abstaining. There were no broker non-votes.

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**ITEM 6. EXHIBITS**

a. Exhibits

10.1 Amendment to Executive Employment Agreement with Richard L. Marcantonio, dated November 16, 2007 (incorporated herein by reference to Registrant's Form 8-K filed November 20, 2007).

10.2 Amendment to Executive Employment Agreement with Douglas A. Milroy, dated November 16, 2007 (incorporated herein by reference to Registrant's Form 8-K filed November 20, 2007).

10.3 Amendment to Executive Employment Agreement with David M. Miller, dated November 16, 2007 (incorporated herein by reference to Registrant's Form 8-K filed November 20, 2007).

10.4 Amendment to Executive Employment Agreement with Robert G. Wood, dated November 16, 2007 (incorporated herein by reference to Registrant's Form 8-K filed November 20, 2007).

10.5 Amendment to Executive Employment Agreement with Jeffrey L. Wright, dated November 16, 2007 (incorporated herein by reference to Registrant's Form 8-K filed November 20, 2007).

31.1 Certification of Chief Executive Officer pursuant to Securities Exchange Act Rule 13a-14(a)/15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of Chief Financial Officer pursuant to Securities Exchange Act Rule 13a-14(a)/15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

G&K SERVICES, INC.  
(Registrant)

Date: February 1, 2008

By: /s/ Jeffrey L. Wright  
Jeffrey L. Wright  
Senior Vice President and  
Chief Financial Officer  
(Principal Financial Officer)

By: /s/ Thomas J. Dietz  
Thomas J. Dietz  
Vice President and Controller  
(Principal Accounting Officer)