C

ANNUAL REPORT 1981

Sklar-Peppler

SKLAR MANUFACTURING LIMITED

DIRECTORS

*DOUGLAS R. ANNETT
Toronto, Ontario
President
Annett Partners Limited

*ALLAN L. BEATTIE, Q.C.
Toronto, Ontario
Managing Partner
Osler, Hoskin & Harcourt

PAUL A. BIENVENU
Montreal, Quebec
President
Howard Bienvenu Inc.

PAUL F. BLACK
Toronto, Ontario
President
Black, Galper & Heessels Limited

**EDWIN T. COHEN
Willowdale, Ontario
Managing Director
ECO Markets Research and Advisory Associates Ltd.

JOSEPH SKLAR
Toronto, Ontario
Senior Vice-President
Sklar Manufacturing Limited

*LOUIS SKLAR
**Oshawa, Ontario
President
Sklar Manufacturing Limited

SAMUEL SKLAR
Toronto, Ontario
Chairman of the Board
Sklar Manufacturing Limited

**JACK B. WHITELY
Oakville, Ontario
Chairman and Chief Executive Officer
Calvert-Dale Estates Ltd.

*Member of Executive Committee
**Member of Audit Committee

OFFICERS

SAMUEL SKLAR
Chairman of the Board

LOUIS SKLAR, B.A.Sc.
President

JOSEPH SKLAR
Senior Vice-President

R.E.G. WILSON, B. Comm., C.A.
Vice-President, Finance and Secretary

J.E.R. DEMERS, R.I.A.
Treasurer

HEAD OFFICE

617 Victoria Street East, Whitby, Ontario L1N 5S7 Telephone (416) 668-3315 or (416) 686-3601

PLANTS

Whitby, Ontario
Weston, Ontario
Hanover, Ontario
Southampton, Ontario

SHOWROOMS

Downsview, Ontario
Montreal, Quebec

TRANSFER AGENT AND REGISTRAR

Montreal Trust Company, Toronto and Montreal

BANKERS

The Royal Bank of Canada

AUDITORS

Soberman, Isenbaum & Colomby

STOCK LISTING

Toronto Stock Exchange (SKM)

PRESIDENT'S REPORT TO SHAREHOLDERS

Having in mind the deterioration of the North American economy and its impact on the home furnishing industry, we are, on the whole, gratified with the operating results of our Company for 1981.

In my 3rd Quarter Report to Shareholders, I identified a decline in consumer demand for home furnishings, which began in the 2nd Quarter of the year. As the year progressed, this decline continued, and by the middle of the 3rd Quarter, it became evident that the improvement in sales, normally experienced in the second half of the year, would not materialize. In fact, the reverse occurred. In the 4th Quarter, this decline in demand accelerated. This situation, together with high inventories at the retail level, resulted in a rapid erosion of order backlogs. During this period, order backlogs at our wood furniture factories would have permitted us to continue normal production levels. However, in early October, an explosion occurred in one of these factories which resulted in a shutdown of all wood furniture manufacturing operations for approximately six weeks. Losses incurred as a result of the explosion are adequately covered by insurance.

I am pleased to be able to report that, despite these reduced levels of production, the Company did record a pretax profit of $470,000 in the 4th Quarter of the year. For 1981, as a whole, because of the record pace that we established for the first three quarters of the year, the Company recorded the highest sales, and the second highest profit (before taxes and extraordinary income) in its history. Net earnings for 1981 of $3,138,000 were, in fact, the highest in our history.

As we enter 1982, we see no signs of a revival in consumer demand for home furnishings. The recession is continuing, and it appears that the entire first half of this year will be a difficult period for our industry, and our Company. Some upward trend in business conditions is anticipated commencing about mid-year. Should this occur, it would result in improved performance in the second half of the year. However, it should be noted that, because of high inventories at the retail level, there would be some time lag between improved consumer demand and increased factory orders.

We believe that this anticipated recovery will continue into 1983, and if this, in fact, occurs, 1983 should be a good year for our Company.

Meanwhile, our approach to the current depressed market is twofold. We are striving for a larger share of the sharply reduced market and, at the same time, we are making every effort to increase operating efficiencies. These efforts will be carried out in a manner that should enable the Company to effectively resume its growth in both sales and earnings when the economy improves.

LOUIS SKLAR
President

March 8, 1982

CONSOLIDATED TEN YEAR SUMMARY

(in thousands of dollars except per common share calculations and other statistics)

	1981	1980	1979	1978	1977	1976	1975	1974	1973	1972
OPERATIONS										
Net sales (excluding discontinued operations)	**$77,172**	$69,795	$59,634	$51,907	$47,401	$47,082	$41,404	$43,429	$38,116	$28,213
Earnings (loss) before taxes and extraordinary items	**4,202**	5,006	2,677	1,765	(3,458)	(692)	(4,025)	1,093	4,276	3,071
Earnings (loss) before extraordinary items	**2,366**	2,611	1,424	950	(3,355)	(770)	(2,781)	385	2,377	1,597
Net earnings (loss)	**3,138**	3,127	2,677	1,879	(4,434)	26	(2,781)	385	2,377	1,770
CAPITAL EXPENDITURES	**2,260**	1,148	379	245	198	480	2,322	3,414	1,405	1,458
FINANCIAL POSITION										
Working capital	**10,881**	13,127	12,117	11,026	3,337	8,042	4,026	7,382	6,630	4,302
Current ratio	**2.26:1**	2.68:1	3.22:1	2.84:1	1.20:1	1.52:1	1.26:1	1.49:1	1.69:1	1.56:1
Fixed assets (net)	**6,470**	3,865	3,198	3,258	6,474	7,131	7,935	6,806	4,436	3,923
Total assets	**27,360**	25,617	21,885	21,436	26,338	30,747	27,765	29,153	20,621	15,891
Long term debt	**5,438**	7,800	10,000	11,700	7,952	8,973	5,885	4,291	1,943	1,868
Shareholders' equity	**12,380**	9,433	6,415	3,738	1,859	6,293	6,149	8,930	8,537	5,997
PER COMMON SHARE										
Basic net earnings (loss) before extraordinary items	**0.98**	1.09	0.59	0.40	(1.40)	(0.32)	(1.16)	0.16	1.02	0.72
Basic net earnings (loss)	**1.30**	1.30	1.11	0.78	(1.85)	0.01	(1.16)	0.16	1.02	0.79
Shareholders' equity	**5.10**	3.92	2.67	1.56	0.77	2.62	2.56	3.72	3.56	2.59
OTHER STATISTICS										
Approximate number of shareholders	**1,070**	1,360	1,500	1,900	2,100	2,150	1,900	1,900	1,900	1,700
Common shares outstanding at year end (000's)	**2,428**	2,408	2,403	2,403	2,403	2,403	2,403	2,403	2,400	2,319

CONSOLIDATED STATEMENT OF EARNINGS

FOR THE YEARS ENDED DECEMBER 31, 1981 and 1980	**1981**	1980
Net sales	**$77,172,000**	$69,795,000
Operating costs and expenses		
Cost of goods sold	**59,009,000**	53,901,000
Marketing, general and administrative	**12,284,000**	10,107,000
Depreciation	**679,000**	481,000
Interest on long term debt net of interest income of $360,000 (1980 - $591,000)	**998,000**	300,000
	72,970,000	64,789,000
Earnings before income taxes and extraordinary income	**4,202,000**	5,006,000
Income taxes		
Current	**1,024,000**	1,566,000
Deferred	**812,000**	829,000
	1,836,000	2,395,000
Earnings before extraordinary income	**2,366,000**	2,611,000
Extraordinary income		
Reduction in current income taxes as a result of loss carry forward	**772,000**	516,000
Net earnings	**$ 3,138,000**	$ 3,127,000
Basic earnings per share (note 8)		
Before extraordinary income	**$ 0.98**	$ 1.09
Net earnings	**1.30**	$ 1.30

See accompanying notes to consolidated financial statements.

AUDITORS' REPORT

To the Shareholders of
Sklar Manufacturing Limited

We have examined the consolidated balance sheet of Sklar Manufacturing Limited as at December 31, 1981 and the consolidated statements of earnings, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1981 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Soberman, Isenbaum and Colomby
Chartered Accountants

Toronto, Canada
February 25, 1982

CONSOLIDATED BALANCE SHEET

AS AT DECEMBER 31, 1981 and 1980

	1981	1980
ASSETS		
Current		
Cash and short term deposits	$ —	$ 3,929,000
Accounts receivable	7,844,000	7,372,000
Inventories (note 3)	11,441,000	9,438,000
Prepaid expenses	235,000	213,000
	19,520,000	20,952,000
Long term receivables (note 4)	1,370,000	800,000
Fixed - at cost (note 5)		
Land	1,156,000	62,000
Buildings and leasehold improvements	5,298,000	4,018,000
Machinery and equipment	6,655,000	5,662,000
	13,109,000	9,742,000
Less: accumulated depreciation	6,639,000	5,877,000
	6,470,000	3,865,000
	$27,360,000	$25,617,000
LIABILITIES		
Current		
Bank indebtedness (note 6)	$ 934,000	$ —
Accounts payable and accrued charges	4,601,000	5,379,000
Sales and other taxes payable	1,148,000	2,055,000
Long term debt due within one year	1,736,000	—
Dividend payable	122,000	121,000
Deferred income taxes - current	98,000	270,000
	8,639,000	7,825,000
Long term debt (note 7)	5,438,000	7,800,000
Deferred income taxes	903,000	559,000
SHAREHOLDERS' EQUITY		
Capital stock (note 8)		
Authorized		
3,500,000 common shares without par value		
Issued		
2,427,769 (1980 - 2,407,569 shares)	7,554,000	7,503,000
Retained earnings	4,826,000	1,930,000
	12,380,000	9,433,000
	$27,360,000	$25,617,000

See accompanying notes to consolidated financial statements.

Approved on behalf of the Board

S. Sklar, Director

J.B. Whitely, Director

CONSOLIDATED STATEMENT OF RETAINED EARNINGS

FOR THE YEARS ENDED DECEMBER 31, 1981 and 1980	1981	1980
Retained earnings (deficit), beginning of year	$1,930,000	($1,076,000)
Add: net earnings	3,138,000	3,127,000
	5,068,000	2,051,000
Deduct: dividends	242,000	121,000
Retained earnings, end of year	$4,826,000	$1,930,000

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

FOR THE YEARS ENDED DECEMBER 31, 1981 and 1980	1981	1980
Source of funds		
Earnings before extraordinary income	$ 2,366,000	$ 2,611,000
Add charges not involving funds		
Depreciation	679,000	481,000
Deferred income taxes - non-current	184,000	559,000
Loss on disposal of fixed assets	26,000	—
Funds provided by operations	3,255,000	3,651,000
Reduction in current income taxes as a result of loss carry forward	772,000	516,000
Reduction in long term receivables	130,000	300,000
Issue of common shares on exercise of employees' stock options	51,000	12,000
	4,208,000	4,479,000
Application of funds		
Long term debt - net	3,102,000	2,200,000
Additions to fixed assets - net	2,260,000	1,148,000
Loans to employees to purchase homes and exercise stock options	700,000	—
Purchase of Heintzman Limited - net of working capital acquired (note 2)	150,000	—
Dividends	242,000	121,000
	6,454,000	3,469,000
Increase (decrease) in working capital	(2,246,000)	1,010,000
Working capital, beginning of year	13,127,000	12,117,000
Working capital, end of year	$10,881,000	$13,127,000

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 1981

1 Summary of significant accounting policies

(a) Principles of consolidation

The consolidated financial statements include the accounts of the company and its subsidiaries, all of which are wholly owned.

(b) Translation of foreign currencies

Current assets and liabilities in foreign currencies are translated into Canadian dollars at the year end exchange rates. The exchange adjustment arising from such translation has been reflected in earnings.

(c) Inventories

Inventories are valued at the lower of cost and net realizable value, with cost determined on a first in, first out basis.

(d) Depreciation

Depreciation is provided in the accounts on the straight line method over the estimated useful lives of the fixed assets as follows:

Buildings —
20 - 40 years

Leasehold improvements —
over the unexpired terms of the leases

Machinery and equipment —
7 - 10 years

(e) Pensions

Substantially all of the company's employees are covered by company pension plans as well as by compulsory government plans. Costs resulting from amendments or improvements to the plans which relate to service of employees in prior years are amortized and funded over periods of not more than fifteen years.

(f) Leases

The company's leases qualify as operating leases and accordingly, all rental payments are expensed as incurred.

2 Acquisition and reorganization

(a) Acquisition of Heintzman Limited

On January 19, 1981, the company acquired all of the outstanding common shares of Heintzman Limited, a company engaged in the manufacture of pianos. Details of the acquisition which was accounted for by the purchase method are as follows:

Assets acquired, at fair value		
Current assets		$ 983,000
Fixed assets		1,050,000
		2,033,000
Liabilities assumed		
Current	$278,000	
Non-current	900,000	1,178,000
Net purchase price settled for cash		$ 855,000

(b) On February 2, 1981, the subsidiary companies were reorganized with the result that Sklar Furniture Limited was wound up and its furniture manufacturing operations continued as divisions of Heintzman Limited.

3 Inventories

These consist of:

	1981	1980
Raw materials	$ 5,509,000	$5,022,000
Work in progress	3,751,000	3,123,000
Finished goods	2,181,000	1,293,000
	$11,441,000	$9,438,000

4 Long term receivables

Consist of:

	1981	1980
Debenture receivable with interest at prime plus 1%, due 1985	$ 800,000	$800,000
Non-interest bearing loans to employees (including $475,000 due from certain officers who are also directors) in connection with:		
Housing mortgage loans maturing on termination of employment, repayable in equal annual installments of 1/25th of the original amount of the loan	658,000	—
Exercise of stock options	42,000	—
	1,500,000	800,000
Less: amounts due within one year included in current assets	130,000	—
	$1,370,000	$800,000

The due dates of the amounts receivable are as follows:

1982	$ 130,000
1983	131,000
1984	131,000
1985	532,000
Subsequent to 1985	576,000
	$1,500,000

5 Fixed assets

During the year the company acquired 6.4 acres of land in Metropolitan Toronto at a cost of $944,000 as a future showroom site. Architectural and other preconstruction costs totalling $127,000 have been capitalized. It is anticipated that construction will commence in 1983.

6 Bank indebtedness

Current bank indebtedness, which bears interest at prime rate, and the bank term loan are secured by the accounts receivable, inventories and the debenture receivable as well as a fixed and floating charge debenture on all other assets.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 1981

7 Long term debt

	1981	1980
Bank term loan due 1985, with interest at 3/4% above prime	$6,300,000	$ —
Debenture payable due 1985, with interest at 12-1/8%	392,000	—
Note payable due 1983, with interest at prime plus 1%	350,000	—
Chattel mortgage due 1984, with interest at 19-3/4%	132,000	—
Bank income debenture converted to a bank term loan on February 2, 1981	—	7,800,000
	7,174,000	7,800,000
Less: amounts due within one year included in current liabilities	1,736,000	—
	$5,438,000	$7,800,000

(a) Payments required to retire long term debt are as follows:

1982	$1,736,000
1983	2,094,000
1984	1,752,000
1985	1,592,000
	$7,174,000

(b) Security

Except for the note payable, which is unsecured, and subject to the assets pledged against bank indebtedness, as referred to in note 6, the remaining long term debt is secured by fixed charges on a building and certain equipment.

(c) Restrictions

The restrictions relating to the long term debt require the company to maintain both working capital and shareholders' equity of $8,000,000 each. There are certain other conditions and restrictions including limitations on the purchase of fixed assets, lease commitments and dividend payments.

8 Capital stock

(a) Options

As at December 31, 1981, 103,200 common shares were reserved for possible issue under the 1979 Key Employees' Stock Option Plan at a price of $2.52 per share. These options may be exercised in annual amounts for the next four years and no shares subject to option may be purchased after March 15, 1986. During 1981 options were exercised for the purchase of 20,200 common shares at a price of $2.52 per share.

(b) Earnings per share

The exercise of all outstanding options would result in fully diluted earnings per share as follows:

Before extraordinary income	$0.94
Net earnings	$1.25

9 Remuneration of directors and senior officers

The total direct remuneration paid or payable by the company and its subsidiaries to its directors and senior officers amounted to $693,000 in 1981 and $652,000 in 1980.

10 Pension plans

Pension costs, including amounts for compulsory government pension plans, were $906,000 in 1981 and $775,000 in 1980. These amounts include current service costs and payments on account of the unfunded liability in respect of past service.

During the year pension benefits were improved, thereby increasing the unfunded past service obligation. Based on the most recent actuarial reviews the unfunded liability for past service amounted to approximately $1,335,000 at December 31, 1981 ($375,000 at December 31, 1980).

11 Commitments and contractual obligations

(a) Long term leases

The company is committed under long term operating leases with various expiry dates to 1995. Minimum rentals (exclusive of taxes, insurance and maintenance costs) for the next five years under these leases are approximately $635,000 annually.

(b) Employment agreements with senior officers

During 1981 the company entered into employment agreements with its five senior officers, terms varying from five to ten years. With respect to compensation, the agreements provide for base salaries, incentive bonuses based on earnings, as well as pension and other benefits. The agreements also provide for severance allowances, the amounts, if any, that may be payable being contingent upon the circumstances leading to the termination of employment and varying from a minimum of six months to a maximum of three years' remuneration.

(c) Housing mortgage loans

At December 31, 1981, there are commitments outstanding to senior officers of the company for the right to obtain interest free housing mortgage loans totalling approximately $500,000 on the same terms as referred to in note 4.

12 Segmented information

The company operates principally in one class of business, that being the manufacture and sale of furniture.

13 Subsequent event

The company is continuing discussions with its principal shareholder, PCL Industries Limited, relating to a possible amalgamation between the companies, however, to date no definite agreement has been reached.