

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

APPLEBEES INTERNATIONAL INC  
Form 10-Q  
May 03, 2001

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934

For the quarterly period ended April 1, 2001  
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OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 000-17962  
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Applebee's International, Inc.  
-----

(Exact name of registrant as specified in its charter)

Delaware  
-----

43-1461763  
-----

(State or other jurisdiction of  
incorporation or organization)

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

4551 W. 107th Street, Suite 100, Overland Park, Kansas 66207  
-----

(Address of principal executive offices and zip code)

(913) 967-4000  
-----

(Registrant's telephone number, including area code)

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   
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The number of shares of the registrant's common stock outstanding as of April 27, 2001 was 24,608,377.

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APPLEBEE'S INTERNATIONAL, INC.  
FORM 10-Q  
FISCAL QUARTER ENDED APRIL 1, 2001  
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APPLEBEE'S INTERNATIONAL, INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS  
(Unaudited)  
(in thousands, except share amounts)

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ASSETS

Current assets:

Cash and cash equivalents.....	\$	10,674
Short-term investments, at market value (amortized cost of \$1,200 in 2001 and \$1,250 in 2000).....		1,254
Receivables (less allowance for bad debts of \$3,587 in 2001 and \$3,137 in 2000)		25,328
Inventories.....		13,016
Prepaid and other current assets.....		6,446
		-----
Total current assets.....		56,718
Property and equipment, net.....		312,688
Goodwill, net.....		81,940
Franchise interest and rights, net.....		2,824
Other assets.....		18,588
		-----
	\$	472,758
		=====

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities:

Current portion of long-term debt.....	\$	896
Accounts payable.....		24,401
Accrued expenses and other current liabilities.....		54,602
Accrued dividends.....		--
Accrued income taxes.....		10,422
		-----
Total current liabilities.....		90,321
		-----

Non-current liabilities:

Long-term debt - less current portion.....		105,466
Deferred income taxes.....		2,425
Other non-current liabilities.....		3,538
		-----
Total non-current liabilities.....		111,429
		-----
Total liabilities.....		201,750
		-----

Commitments and contingencies (Note 2)

Stockholders' equity:

Preferred stock - par value \$0.01 per share: authorized - 1,000,000 shares; no shares issued.....		--
Common stock - par value \$0.01 per share: authorized - 125,000,000 shares; issued - 32,150,360 shares.....		321
Additional paid-in capital.....		173,503
Retained earnings.....		310,714
Accumulated other comprehensive income (loss), net of income taxes.....		(1,274)
		-----
		483,264
Treasury stock - 7,717,039 shares in 2001 and 6,930,530 shares in 2000, at cost.		(212,256)
		-----
Total stockholders' equity.....		271,008
		-----
	\$	472,758
		=====

See notes to consolidated financial statements.

APPLEBEE'S INTERNATIONAL, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF EARNINGS  
(Unaudited)  
(in thousands, except per share amounts)

	13 Weeks Ended	
	April 1, 2001	March 2001
	-----	-----
Revenues:		
Company restaurant sales.....	\$ 160,143	\$ 143,111
Franchise income.....	22,234	18,111
	-----	-----
Total operating revenues.....	182,377	161,222
	-----	-----
Cost of company restaurant sales:		
Food and beverage.....	43,305	43,305
Labor.....	50,900	49,900
Direct and occupancy.....	40,759	39,759
Pre-opening expense.....	135	135
	-----	-----
Total cost of company restaurant sales.....	135,099	133,100
	-----	-----
General and administrative expenses.....	17,166	17,166
Amortization of intangible assets.....	1,463	1,463
Loss on disposition of restaurants and equipment.....	187	187
	-----	-----
Operating earnings.....	28,462	26,522
	-----	-----
Other income (expense):		
Investment income.....	357	357
Interest expense.....	(2,357)	(2,357)
Other income.....	90	90
	-----	-----
Total other expense.....	(1,910)	(1,910)
	-----	-----
Earnings before income taxes.....	26,552	24,612
Income taxes.....	9,771	9,771
	-----	-----
Net earnings.....	\$ 16,781	\$ 14,841
	=====	=====
Basic net earnings per common share.....	\$ 0.68	\$ 0.67
	=====	=====
Diluted net earnings per common share.....	\$ 0.67	\$ 0.66
	=====	=====
Basic weighted average shares outstanding.....	24,744	22,312
	=====	=====
Diluted weighted average shares outstanding.....	25,085	22,312
	=====	=====

See notes to consolidated financial statements.

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APPLEBEE'S INTERNATIONAL, INC. AND SUBSIDIARIES  
 CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY  
 (Unaudited)  
 (in thousands, except share amounts)

	Common Stock		Additional	Retained	Accumula
	Shares	Amount	Paid-In Capital	Earnings	Other Comprehen Income (L
	-----	-----	-----	-----	-----
Balance, December 31, 2000.....	32,150,360	\$ 321	\$ 172,037	\$ 293,933	\$ 3
Comprehensive income:					
Net earnings.....	--	--	--	16,781	--
Change in unrealized gain on short-term investments, net of income taxes.....	--	--	--	--	(
Fair value of financial instruments, net of income taxes.....	--	--	--	--	(1,30
Total comprehensive income.....	--	--	--	16,781	(1,31
Purchases of treasury stock....	--	--	--	--	--
Stock options exercised and related tax benefit.....	--	--	693	--	--
Shares issued under employee stock and 401(k) plans.....	--	--	526	--	--
Restricted stock shares awarded under equity incentive plan, net of cancellations.....	--	--	(66)	--	--
Unearned compensation relating to restricted shares.....	--	--	83	--	--
Notes receivable from officers for stock sales.....	--	--	230	--	--
Balance, April 1, 2001.....	32,150,360	\$ 321	\$ 173,503	\$ 310,714	\$ (1,27

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See notes to consolidated financial statements.

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APPLEBEE'S INTERNATIONAL, INC. AND SUBSIDIARIES  
 CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (Unaudited)  
 (in thousands)

	13 We
	-----
	April 1,
	2001
	-----
CASH FLOWS FROM OPERATING ACTIVITIES:	
Net earnings.....	\$ 16,781
Adjustments to reconcile net earnings to net cash provided by operating activities:	
Depreciation and amortization.....	7,781
Amortization of intangible assets.....	1,463
Amortization of deferred financing costs.....	180
Deferred income tax provision (benefit).....	(1,657)
Loss on disposition of restaurants and equipment.....	187
Changes in assets and liabilities:	
Receivables.....	(3,227)
Inventories.....	(400)
Prepaid and other current assets.....	691
Accounts payable.....	(2,155)
Accrued expenses and other current liabilities.....	(6,882)
Accrued income taxes.....	9,322
Other non-current liabilities.....	(127)
Other.....	(381)
	-----
NET CASH PROVIDED BY OPERATING ACTIVITIES.....	21,576
	-----
CASH FLOWS FROM INVESTING ACTIVITIES:	
Purchases of property and equipment.....	(6,438)
Proceeds from sale of restaurants and equipment.....	14
Purchases of short-term investments.....	(49)
Maturities of short-term investments.....	100
	-----
NET CASH USED BY INVESTING ACTIVITIES.....	(6,373)
	-----
CASH FLOWS FROM FINANCING ACTIVITIES:	
Purchases of treasury stock.....	(29,525)
Dividends paid.....	(2,774)
Issuance of common stock upon exercise of stock options.....	1,796
Shares sold under employee stock purchase plan.....	211
Proceeds from issuance of long-term debt.....	15,000
Payments on long-term debt.....	--
	-----

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NET CASH USED BY FINANCING ACTIVITIES.....	(15,292)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS.....	(89)
CASH AND CASH EQUIVALENTS, beginning of period.....	10,763
CASH AND CASH EQUIVALENTS, end of period.....	\$ 10,674

See notes to consolidated financial statements.

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APPLEBEE'S INTERNATIONAL, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS - (Continued)  
(Unaudited)  
(in thousands)

	13 Wee
	April 1, 2001
Supplemental disclosures of cash flow information:	
Cash paid during the 13 week period for:	
Income taxes.....	\$ 2,748
Interest.....	\$ 2,079

Disclosure of Accounting Policy:

For purposes of the consolidated statements of cash flows, the Company considers all highly liquid investments purchased with a maturity of three months or less to be cash equivalents.

See notes to consolidated financial statements.

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APPLEBEE'S INTERNATIONAL, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

1. Basis of Presentation

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Our consolidated financial statements included in this Form 10-Q have been prepared without audit (except that the balance sheet information as of December 31, 2000 has been derived from consolidated financial statements which were audited) in accordance with the rules and regulations of the Securities and Exchange Commission. Although certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted, we believe that the disclosures are adequate to make the information presented not misleading. The accompanying consolidated financial statements should be read in conjunction with the audited financial statements and notes thereto included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2000.

We believe that all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the results of the interim periods presented have been made. The results of operations for the interim periods presented are not necessarily indicative of the results to be expected for the full year.

### 2. Commitments and Contingencies

**Litigation, claims and disputes:** As of April 1, 2001, we were using assets owned by a former franchisee in the operation of one restaurant. That restaurant remains under a purchase rights agreement that required us to make certain payments to the franchisee's lender. In 1991, a dispute arose between the lender and us over the amount of the payments due the lender under that agreement and over whether we had agreed to guarantee the franchisee's debt. Based upon a then-current independent appraisal, we offered to settle the dispute and purchase the assets of the three then-existing restaurants for \$1,000,000 in 1991. In November 1992, the FDIC declared the lender insolvent, and the lender has since been liquidated. We closed one of the three restaurants in 1994 and one of the two remaining restaurants in February 1996. In the fourth quarter of 1996, we received information indicating that a third party had acquired the franchisee's indebtedness to the FDIC. In June 1997, the third party filed a lawsuit against us seeking approximately \$3,800,000. In April 1999, the district court awarded a summary judgment of \$3,833,000 to the third party. In June 2000, the court of appeals reversed the summary judgment and remanded the case to the district court for further action. The third party appealed the court's decision but its appeal was denied. This case is currently pending in the district court. As of April 1, 2001, we believe we have recorded adequate reserves for this matter.

In addition, we are involved in various legal actions arising in the normal course of business. These matters include disputes with certain international franchisees regarding disclosures we allegedly made or omitted. We have also filed claims against these franchisees for amounts due. These matters are in the initial stages of assessment; however, we believe that we have meritorious defenses to the allegations of the franchisees and are vigorously defending these claims.

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While the resolution of the matters described above may have an impact on the financial results for the period in which they are resolved, we believe that the ultimate disposition of these matters will not, in the aggregate, have a material adverse effect upon our business or consolidated financial position.

**Franchise financing:** In 1992, we entered into an agreement with a financing source to provide up to \$75,000,000 of financing to our franchisees to fund development of new franchise restaurants. We provided a limited guaranty of



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loans made under the agreement. Our maximum recourse obligation for each long-term loan is 10% of the amount funded, and this is gradually reduced beginning in the second year of each loan. After the seventh year of each loan, it decreases to zero. Approximately \$49,000,000 was funded through this financing source. Of this, approximately \$3,000,000 was outstanding as of April 1, 2001. This agreement expired on December 31, 1994 and was not renewed.

**Lease guaranties:** In connection with the sale of restaurants to franchisees and other parties, we have, in certain cases, remained contingently liable for the remaining lease payments. As of April 1, 2001, the aggregate amount of these lease payments totaled approximately \$29,800,000. The buyers have indemnified us from any losses related to these guaranties.

**Philadelphia divestiture:** In connection with the sale of the Philadelphia restaurants, we provided a guarantee to a franchise group totaling \$1,250,000. As of April 1, 2001, \$718,000 remains outstanding.

**Severance agreements:** We have severance and employment agreements with certain officers providing for severance payments to be made in the event the employee resigns or is terminated related to a change in control. The agreements define the circumstances which will constitute a change in control. If the severance payments had been due as of April 1, 2001, we would have been required to make payments totaling approximately \$6,800,000. In addition, we have severance and employment agreements with certain officers which contain severance provisions not related to a change in control. Those provisions would have required aggregate payments of approximately \$4,300,000 if such officers had been terminated as of April 1, 2001.

### 3. Earnings Per Share

We compute basic earnings per share by dividing income available to common shareholders by the weighted average number of common shares outstanding for the reporting period. Diluted earnings per share reflects the potential dilution that could occur if holders of options or other contracts to issue common stock exercised or converted their holdings into common stock. Outstanding stock options represent the only dilutive effects on weighted average shares. The chart below presents a reconciliation between basic and diluted weighted average shares outstanding and the related earnings per share. All amounts in the chart except per share amounts are expressed in thousands.

	13 Weeks Ended	
	April 1, 2001	Mar 2
Net earnings.....	\$ 16,781	\$
Basic weighted average shares outstanding.....	24,744	
Dilutive effect of stock options.....	341	

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Diluted weighted average shares outstanding.....	25,085	
=====		
Basic net earnings per common share.....	\$ 0.68	\$
=====		
Diluted net earnings per common share.....	\$ 0.67	\$
=====		

#### 4. New Accounting Pronouncement

Effective January 1, 2001, we adopted the provisions of SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" issued by the Financial Accounting Standards Board. SFAS No. 133, as amended by SFAS Nos. 137 and 138, establishes accounting and reporting standards for derivative instruments and hedging activities. It requires an entity to recognize all derivatives as either assets or liabilities on the balance sheet. The statement also requires changes in the fair value of the derivative instruments to be recorded in either net earnings or other comprehensive income depending on their intended use.

We have interest rate swap agreements to manage our exposure to interest rate fluctuations. The swap agreements effectively fix the underlying three-month LIBOR interest rate on \$75,000,000 of our senior credit facilities to rates ranging from 5.91% to 6.05%. The estimated fair value of these agreements at April 1, 2001 was a net payable of \$2,069,000 and is included in other non-current liabilities on the accompanying balance sheets. Our interest rate swap agreements meet the criteria for hedge accounting under SFAS No. 133 and accordingly, the cumulative after-tax fair value of the interest rate hedges is included as a reduction in other comprehensive income in the first quarter of 2001.

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#### Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

##### General

Our revenues are generated from two primary sources:

- o Company restaurant sales (food and beverage sales)
- o Franchise income

Franchise income consists of franchise restaurant royalties (generally 4% of each franchise restaurant's monthly gross sales) and franchise fees (which typically range from \$30,000 to \$35,000 for each restaurant opened). Beverage sales include sales of alcoholic beverages, while non-alcoholic beverages are included in food sales.

Certain expenses relate only to company operated restaurants. These include:

- o food and beverage costs
- o labor costs
- o direct and occupancy costs
- o pre-opening expenses

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Other expenses, such as general and administrative and amortization expenses, relate to both company operated restaurants and franchise operations.

We operate on a 52 or 53 week fiscal year ending on the last Sunday in December. Our fiscal quarters ended April 1, 2001 and March 26, 2000 each contained 13 weeks and are referred to hereafter as the "2001 quarter" and the "2000 quarter", respectively.

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### Results of Operations

The following table contains information derived from our consolidated statements of earnings expressed as a percentage of total operating revenues, except where otherwise noted. Percentages may not add due to rounding.

	13 Weeks Ende	
	April 1, 2001	Ma
	-----	-----
Revenues:		
Company restaurant sales.....	87.8%	
Franchise income.....	12.2	
	-----	-----
Total operating revenues.....	100.0%	
	=====	=====
Cost of sales (as a percentage of company restaurant sales):		
Food and beverage.....	27.0%	
Labor.....	31.8	
Direct and occupancy.....	25.5	
Pre-opening expense.....	0.1	
	-----	-----
Total cost of sales.....	84.4%	
	=====	=====
General and administrative expenses.....	9.4%	
Amortization of intangible assets.....	0.8	
Loss on disposition of restaurants and equipment.....	0.1	
	-----	-----
Operating earnings.....	15.6	
	-----	-----
Other income (expense):		
Investment income.....	0.2	
Interest expense.....	(1.3)	
Other income.....	--	
	-----	-----
Total other expense.....	(1.0)	
	-----	-----
Earnings before income taxes.....	14.6	
Income taxes.....	5.4	
	-----	-----
Net earnings.....	9.2%	
	=====	=====

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The following table sets forth certain unaudited financial information and other restaurant data relating to company and franchise restaurants, as reported to us by franchisees:

	13 Weeks
	----- April 1, 2001 -----
Number of restaurants:	
Company(1):	
Beginning of period.....	285
Restaurant openings.....	2
Restaurant closings.....	--
End of period.....	----- 287 -----
Franchise:	
Beginning of period.....	1,001
Restaurant openings.....	12
Restaurant closings.....	(1)
End of period.....	----- 1,012 -----
Total:	
Beginning of period.....	1,286
Restaurant openings.....	14
Restaurant closings.....	(1)
End of period.....	----- 1,299 =====
Weighted average weekly sales per restaurant:	
Company(1).....	\$ 42,968
Franchise.....	\$ 42,328
Total.....	\$ 42,470
Change in comparable restaurant sales:(2)	
Company(1).....	3.6%
Franchise.....	3.1%
Total.....	3.2%
Total system sales (in thousands).....	\$ 712,949

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Company Restaurant Sales. Total company restaurant sales increased \$14,692,000

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(10%) from \$145,451,000 in the 2000 quarter to \$160,143,000 in the 2001 quarter due primarily to company restaurant openings and increases in comparable restaurant sales. Comparable restaurant sales at company restaurants increased by 3.6% in the 2001 quarter. Weighted average weekly sales at company restaurants increased 1.4% from \$42,369 in the 2000 quarter to \$42,968 in the 2001 quarter. These increases were due primarily to an increase in the average guest check resulting from the company's food promotions, a menu price increase of approximately 1.8% in the 2001 quarter and increased sales of appetizers, drinks and desserts.

Franchise Income. Overall franchise income increased \$2,435,000 (12%) from \$19,799,000 in the 2000 quarter to \$22,234,000 in the 2001 quarter due primarily to the increased number of franchise restaurants operating during 2001 as compared to 2000 and increases in comparable restaurant sales. Comparable restaurant sales and weighted average weekly sales for franchise restaurants increased 3.1% and 2.1%, respectively, in the 2001 quarter.

Cost of Company Restaurant Sales. Food and beverage costs decreased from 27.5% in the 2000 quarter to 27.0% in the 2001 quarter, due primarily to a menu price increase in the 2001 quarter and operational improvements including the implementation of a new theoretical food cost system in the second quarter of 2000.

Labor costs increased from 31.7% in the 2000 quarter to 31.8% in the 2001 quarter. This increase was due primarily to higher group insurance costs and continued pressure on management costs due to low unemployment as well as the highly competitive nature of the restaurant industry.

Direct and occupancy costs increased from 24.5% in the 2000 quarter to 25.5% in the 2001 quarter due primarily to higher utility costs and smallwares expense. This increase was partially offset by a decrease in advertising costs, as a percentage of sales, due to the timing of food promotions.

General and Administrative Expenses. General and administrative expenses decreased in the 2001 quarter to 9.4% from 9.7% in the 2000 quarter, due primarily to the absorption of general and administrative expenses over a larger revenue base.

Income Taxes. The effective income tax rate, as a percentage of earnings before income taxes, was 36.8% in both the 2000 quarter and 2001 quarter.

### Liquidity and Capital Resources

Our need for capital resources historically has resulted from the construction and acquisition of restaurants. For the foreseeable future, this should continue to be the case. In the past, we have obtained capital through public stock offerings, debt financing, and our ongoing operations. Income from our ongoing operations includes cash generated from company and franchise operations, credit from trade suppliers, real estate lease financing, and landlord contributions to leasehold improvements. We have also used our common stock as consideration in the acquisition of restaurants. In addition, we have assumed debt or issued new debt in connection with certain mergers and acquisitions.

Capital expenditures were \$46,220,000 in fiscal year 2000 and \$6,438,000 in the 2001 quarter. We currently expect to open approximately 25 restaurants in 2001. Capital expenditures are expected to be between \$50,000,000 and \$55,000,000 in

fiscal 2001. These expenditures will primarily be for the development of new

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restaurants, refurbishment and capital replacement for existing restaurants, and the enhancement of information systems. Because we expect to continue to purchase a portion of our sites, the amount of actual capital expenditures will be dependent upon, among other things, the proportion of leased versus owned properties. In addition, if we open more restaurants than we currently anticipate or acquire additional restaurants, our capital requirements will increase accordingly.

Our senior term loan and working capital facilities are subject to various covenants and restrictions which, among other things, require the maintenance of stipulated fixed charge, interest coverage and leverage ratios, as defined, and limit additional indebtedness and capital expenditures in excess of specified amounts. The credit agreement permits annual cash dividends of the greater of \$5,000,000 or 50% of consolidated net income. In addition, in April 2000, the credit agreement was amended to permit additional repurchases of common stock of up to \$50,000,000 through December 31, 2001. We are currently in compliance with the covenants contained in our credit agreement.

In February 2001, our Board of Directors authorized the repurchase of up to \$55,000,000 of our common stock through 2001, subject to market conditions and applicable restrictions imposed by our credit agreement. We repurchased 890,000 shares of our common stock at an average price of \$33.16 per share for an aggregate cost of \$29,525,000 in the 2001 quarter, including \$18,912,000 under this authorization and \$10,613,000 under previous authorizations.

As of April 1, 2001, our liquid assets totaled \$11,928,000. These assets consisted of cash and cash equivalents in the amount of \$10,674,000 and short-term investments in the amount of \$1,254,000. The working capital deficit decreased from \$40,654,000 as of December 31, 2000 to \$33,603,000 as of April 1, 2001. This decrease was due primarily to the redemption of gift certificates sold in 2000, the payment of accrued bonuses and the payment of our annual dividend in January 2001. As of April 1, 2001, \$18,000,000 was outstanding under our working capital and line of credit facilities, and standby letters of credit totaling \$6,413,000 were outstanding under our letter of credit facilities.

We believe that our liquid assets and cash generated from operations, combined with borrowings available under our credit facilities, will provide sufficient funds for our operating, capital and other requirements for the foreseeable future.

### Inflation

Substantial increases in costs and expenses could impact our operating results to the extent such increases cannot be passed along to customers. In particular, increases in food, supplies, labor and operating expenses could have a significant impact on our operating results. We do not believe that inflation has materially affected our operating results during the past three years.

A majority of our employees are paid hourly rates related to federal and state minimum wage laws and various laws that allow for credits to that wage. The Federal government continues to consider an increase in the minimum wage. Several state governments have increased the minimum wage and other state governments are also discussing an increased minimum wage. In the past, we have been able to pass along cost increases to customers through food and beverage price increases, and we will attempt to do so in the future. We cannot guarantee, however, that all future cost increases can be reflected in our prices or that increased prices will be absorbed by customers without at least somewhat diminishing customer spending in our restaurants.

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### New Accounting Pronouncement

Effective January 1, 2001, we adopted the provisions of SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" issued by the Financial Accounting Standards Board. SFAS No. 133, as amended by SFAS Nos. 137 and 138, establishes accounting and reporting standards for derivative instruments and hedging activities. It requires an entity to recognize all derivatives as either assets or liabilities on the balance sheet. The statement also requires changes in the fair value of the derivative instruments to be recorded in either net earnings or other comprehensive income depending on their intended use.

We have interest rate swap agreements to manage our exposure to interest rate fluctuations. The swap agreements effectively fix the underlying three-month LIBOR interest rate on \$75,000,000 of our senior credit facilities to rates ranging from 5.91% to 6.05%. The estimated fair value of these agreements at April 1, 2001 was a net payable of \$2,069,000 and is included in other non-current liabilities on the accompanying balance sheets. Our interest rate swap agreements meet the criteria for hedge accounting under SFAS No. 133 and accordingly, the cumulative after-tax fair value of the interest rate hedges is included as a reduction in other comprehensive income in the first quarter of 2001.

### Forward-Looking Statements

The statements contained in the "Management's Discussion and Analysis of Financial Condition and Results of Operations" section regarding restaurant development and capital expenditures are forward-looking and based on current expectations. There are several risks and uncertainties that could cause actual results to differ materially from those described. These risks include but are not limited to the impact of intense competition in the casual dining segment of the restaurant industry and our ability to control restaurant operating costs which are impacted by market changes, minimum wage and other employment laws, food costs and inflation. For a more detailed discussion of the principal factors that could cause actual results to be materially different, you should read our current report on Form 8-K which we filed with the Securities and Exchange Commission on February 13, 2001. We disclaim any obligation to update forward-looking statements.

### Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Our senior term loan bears interest at either the bank's prime rate plus 1.25% or LIBOR plus 2.25%, at our option. Our working capital facility bears interest at either the bank's prime rate plus 0.125% or LIBOR plus 1.125%, at our option. The interest rate on the working capital facility is subject to change based upon our leverage ratio.

We have interest rate swap agreements in place to manage our exposure to interest rate fluctuations. The swap agreements effectively fix the underlying three-month LIBOR interest rate on \$75,000,000 of the senior credit facilities to rates ranging from 5.91% to 6.05%.

As of April 1, 2001, the total amount of debt subject to interest rate fluctuations was \$26,802,000. This amount was comprised of \$8,802,000 under the term loan and \$18,000,000 under the working capital facility. A 1% change in interest rates would result in an increase or decrease in interest expense of \$268,000 per year.

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### PART II. OTHER INFORMATION

#### Item 1. Legal Proceedings

As of April 1, 2001, we were using assets owned by a former franchisee in the operation of one restaurant. That restaurant remains under a purchase rights agreement that required us to make certain payments to the franchisee's lender. In 1991, a dispute arose between the lender and us over the amount of the payments due the lender under that agreement and over whether we had agreed to guarantee the franchisee's debt. Based upon a then-current independent appraisal, we offered to settle the dispute and purchase the assets of the three then-existing restaurants for \$1,000,000 in 1991. In November 1992, the FDIC declared the lender insolvent, and the lender has since been liquidated. We closed one of the three restaurants in 1994 and one of the two remaining restaurants in February 1996. In the fourth quarter of 1996, we received information indicating that a third party had acquired the franchisee's indebtedness to the FDIC. In June 1997, the third party filed a lawsuit against us seeking approximately \$3,800,000. In April 1999, the district court awarded a summary judgment of \$3,833,000 to the third party. In June 2000, the court of appeals reversed the summary judgment and remanded the case to the district court for further action. The third party appealed the court's decision but its appeal was denied. This case is currently pending in the district court. As of April 1, 2001, we believe we have recorded adequate reserves for this matter.

In addition, we are involved in various legal actions arising in the normal course of business. These matters include disputes with certain international franchisees regarding disclosures we allegedly made or omitted. We have also filed claims against these franchisees for amounts due. These matters are in the initial stages of assessment; however, we believe that we have meritorious defenses to the allegations of the franchisees and are vigorously defending these claims.

While the resolution of the matters described above may have an impact on the financial results for the period in which they are resolved, we believe that the ultimate disposition of these matters will not, in the aggregate, have a material adverse effect upon our business or consolidated financial position.

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#### Item 6. Exhibits and Reports on Form 8-K

- (a) The Exhibits listed on the accompanying Exhibit Index are filed as part of this report.
- (b) We filed a report on Form 8-K on January 17, 2001 announcing an addition to our executive team and a CEO succession plan.
- (c) We filed a report on Form 8-K on January 17, 2001 confirming EPS guidance and announcing sales for the fourth quarter.
- (d) We filed a report on Form 8-K on February 7, 2001 announcing a new \$55 million stock repurchase program and that the previously announced repurchase programs were complete.



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- (e) We filed a report on Form 8-K on February 13, 2001 in accordance with the Private Securities Litigation Reform Act of 1995 as it relates to a safe harbor for companies making forward-looking statements. The factors listed in the report are important factors that could cause actual results to differ materially from those we project in forward-looking statements.
- (f) We filed a report on Form 8-K on February 15, 2001 reporting fourth quarter earnings per share of 63 cents and an EPS increase of 20 percent in 2000 to \$2.40.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

APPLEBEE'S INTERNATIONAL, INC.  
(Registrant)

Date: May 2, 2001  
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By: /s/ Lloyd L. Hill  
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Lloyd L. Hill  
Chairman and Chief Executive Officer  
(principal executive officer)

Date: May 2, 2001  
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By: /s/ George D. Shadid  
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George D. Shadid  
Executive Vice President and  
Chief Financial Officer  
(principal financial officer)

Date: May 2, 2001  
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By: /s/ Mark A. Peterson  
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Mark A. Peterson  
Vice President and Controller  
(principal accounting officer)

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APPLEBEE'S INTERNATIONAL, INC.  
EXHIBIT INDEX

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Exhibit  
Number

Description of Exhibit

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None