

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

APPLEBEES INTERNATIONAL INC
Form 10-Q
July 31, 2003

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 June 29, 2003

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

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

Indicate by check mark whether the registrant is an accelerated filer (as defined by Rule 12b-2 of the Act). Yes No

The number of shares of the registrant's common stock outstanding as of July 24, 2003 was 55,838,740.

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

APPLEBEE'S INTERNATIONAL, INC. AND SUBSIDIARIES
FORM 10-Q
FISCAL QUARTER ENDED JUNE 29, 2003
INDEX

Part I	Financial Information
Item 1.	Consolidated Financial Statements:
	Consolidated Balance Sheets as of June 29, 2003 and December 29, 2002.....
	Consolidated Statements of Earnings for the 13 Weeks and 26 Weeks Ended June 29, 2003 and June 30, 2002.....
	Consolidated Statement of Stockholders' Equity for the 26 Weeks Ended June 29, 2003.....
	Consolidated Statements of Cash Flows for the 26 Weeks Ended June 29, 2003 and June 30, 2002
	Notes to Consolidated Financial Statements.....
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations.....
Item 3.	Quantitative and Qualitative Disclosures About Market Risk.....
Item 4.	Controls and Procedures.....
Part II	Other Information
Item 1.	Legal Proceedings.....
Item 4.	Submission of Matters to a Vote of Security Holders.....
Item 6.	Exhibits and Reports on Form 8-K.....
Signatures
Exhibit Index

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

(Unaudited)
(in thousands, except share amounts)

	June 20
ASSETS	
Current assets:	
Cash and cash equivalents.....	\$
Short-term investments, at market value (amortized cost of \$478 in 2002).....	
Receivables (less allowance for bad debts of \$3,955 in 2003 and \$4,089 in 2002)..	
Receivables related to captive insurance subsidiary.....	
Inventories.....	
Prepaid income taxes.....	
Prepaid and other current assets.....	
Total current assets.....	-----
Property and equipment, net.....	3
Goodwill.....	1
Franchise interest and rights, net.....	
Other assets, net.....	

	\$ 5
	=====
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities:	
Current portion of long-term debt.....	\$
Accounts payable.....	
Accrued expenses and other current liabilities.....	
Loss reserve and unearned premiums related to captive insurance subsidiary.....	
Accrued dividends.....	
Total current liabilities.....	-----
Non-current liabilities:	
Long-term debt - less current portion.....	
Other non-current liabilities.....	
Total non-current liabilities.....	-----
Total liabilities.....	-----
Total liabilities.....	1
Commitments and contingencies (Note 3)	
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 - 72,336,788 shares.....	
Additional paid-in capital.....	1
Retained earnings.....	4
Accumulated other comprehensive income, net of income taxes.....	

	6
Treasury stock - 16,579,329 shares in 2003 and 16,948,371 shares in 2002, at cost.....	(2)
Total stockholders' equity.....	-----
	4

See notes to consolidated financial statements.

3

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

	13 Weeks Ended	
	June 29, 2003	June 30, 2002
Revenues:		
Company restaurant sales	\$ 220,107	\$ 178,893
Franchise royalties and fees.....	27,331	25,484
Other franchise income.....	3,268	463
	-----	-----
Total operating revenues.....	250,706	204,840
	-----	-----
Cost of company restaurant sales:		
Food and beverage.....	57,040	47,073
Labor.....	71,804	58,881
Direct and occupancy.....	54,386	44,291
Pre-opening expense.....	334	305
	-----	-----
Total cost of company restaurant sales.....	183,564	150,550
	-----	-----
Cost of other franchise income.....	3,173	93
General and administrative expenses.....	22,887	19,923
Amortization of intangible assets.....	92	52
Loss on disposition of restaurants and equipment.....	731	727
	-----	-----
Operating earnings.....	40,259	33,495
	-----	-----
Other income (expense):		
Investment income.....	485	381
Interest expense.....	(518)	(555)
Impairment of Chevys note receivable (Note 6)...	(8,803)	--
Other income.....	1	482
	-----	-----
Total other income (expense).....	(8,835)	308
	-----	-----
Earnings before income taxes.....	31,424	33,803
Income taxes.....	11,239	12,338
	-----	-----
Net earnings.....	\$ 20,185	\$ 21,465
	=====	=====
Basic net earnings per common share.....	\$ 0.36	\$ 0.38

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

Diluted net earnings per common share.....	\$ 0.35	\$ 0.37
Basic weighted average shares outstanding.....	55,435	55,872
Diluted weighted average shares outstanding.....	57,032	57,374

See notes to consolidated financial statements.

4

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

	Common Stock		Additional	Retained	Accumulated
	Shares	Amount	Paid-In Capital	Earnings	Other Comprehens Income (Lo
Balance, December 29, 2002.....	72,336,788	\$ 723	\$ 187,523	\$ 434,621	\$ 16
Comprehensive income:					
Net earnings.....	--	--	--	44,787	--
Change in unrealized gain on short-term investments, net of income taxes.....	--	--	--	--	(16
Total comprehensive income.....	--	--	--	44,787	(16
Purchases of treasury stock....	--	--	--	--	--
Stock options exercised and related tax benefit.....	--	--	5,441	--	--
Shares issued under employee stock and 401(k) plans.....	--	--	1,619	--	--
Restricted shares awarded under equity incentive plan..	--	--	(540)	--	--
Unearned compensation relating to restricted shares.....	--	--	539	--	--
Repayments of notes receivable from officers for stock sales	--	--	46	--	--
Balance, June 29, 2003.....	72,336,788	\$ 723	\$ 194,628	\$ 479,408	\$ --

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

See notes to consolidated financial statements.

5

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

	June 29 2003
CASH FLOWS FROM OPERATING ACTIVITIES:	
Net earnings.....	\$ 44,7
Adjustments to reconcile net earnings to net cash provided by operating activities:	
Depreciation and amortization.....	19,9
Amortization of intangible assets.....	1
Amortization of deferred financing costs.....	(7)
Deferred income tax provision (benefit).....	(1)
Gain on sale of investments.....	1,1
Loss on disposition of restaurants and equipment.....	8,8
Impairment of Chevys note receivable.....	3,8
Income tax benefit from exercise of stock options.....	(5,3)
Changes in assets and liabilities (exclusive of effects of acquisition):	
Receivables.....	(4,3)
Receivables related to captive insurance subsidiary.....	(8,0)
Inventories.....	1,8
Prepaid income taxes.....	3
Prepaid and other current assets.....	2,5
Accounts payable.....	(6,6)
Accrued expenses and other current liabilities.....	8,2
Loss reserve and unearned premiums related to captive insurance subsidiary..	--
Accrued income taxes.....	(1,3)
Other.....	65,2
NET CASH PROVIDED BY OPERATING ACTIVITIES.....	(28,9)
CASH FLOWS FROM INVESTING ACTIVITIES:	
Purchases of property and equipment.....	(21,5)
Acquisition of restaurants.....	--
Proceeds from sale of restaurants and equipment.....	4
Purchases of short-term investments.....	(50,0)
Maturities and sales of short-term investments.....	(13,2)
NET CASH USED BY INVESTING ACTIVITIES.....	(3,3)
CASH FLOWS FROM FINANCING ACTIVITIES:	
Purchases of treasury stock.....	8,3
Dividends paid.....	1,4
Issuance of common stock upon exercise of stock options.....	
Shares sold under employee stock purchase plan.....	

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

Net payments on long-term debt.....	(19,0

NET CASH USED BY FINANCING ACTIVITIES.....	(25,8

NET DECREASE IN CASH AND CASH EQUIVALENTS.....	(10,6
CASH AND CASH EQUIVALENTS, beginning of period.....	15,1

CASH AND CASH EQUIVALENTS, end of period.....	\$ 4,5
	=====

See notes to consolidated financial statements.

6

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

	2

	June 29, 2003

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:	
Cash paid during the 26 week period for:	
Income taxes.....	\$ 20,7
	=====
Interest.....	\$ 7
	=====

SUPPLEMENTAL DISCLOSURES OF NONCASH INVESTING AND FINANCING ACTIVITIES:

We issued restricted common stock of \$1,666,000 and \$256,000 for the 26 weeks ended June 29, 2003 and June 30, 2002, respectively.

On March 24, 2003, we assumed a loan of approximately \$1,400,000 in connection with the acquisition of 11 restaurants.

DISCLOSURE OF ACCOUNTING POLICY:

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

See notes to consolidated financial statements.

7

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

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

1. Basis of Presentation

Our consolidated financial statements included in this Form 10-Q have been prepared without audit (except that the balance sheet information as of December 29, 2002 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 29, 2002.

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.

We have made certain reclassifications to the consolidated financial statements to conform to the 2003 presentation.

2. Stock-Based Compensation

We have adopted the disclosure provisions of Statement of Financial Accounting Standards ("SFAS") No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure, an amendment of FASB Statement No. 123." The Statement requires prominent disclosures in both annual and interim financial statements regarding the method of accounting for stock-based employee compensation and the effect of the method used on reported results. We account for stock-based compensation awards under the intrinsic method of Accounting Principles Board Opinion No. 25. Opinion No. 25 requires compensation cost to be recognized based on the excess, if any, between the quoted market price of the stock at the date of grant and the amount an employee must pay to acquire the stock. All options awarded under all of our plans are granted with an exercise price equal to the fair market value on the date of the grant. The following table presents the effect on our net earnings and earnings per share had we adopted the fair value method of accounting for stock-based compensation under SFAS No. 123, "Accounting for Stock-Based Compensation" (in thousands, except for per share amounts).

8

	13 Weeks Ended		26
	June 29, 2003	June 30, 2002	June 29 2003
Net earnings, as reported.....	\$ 20,185	\$ 21,465	\$ 44,78

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

Less: Total stock-based employee compensation expense determined under fair value based methods for all awards, net of related taxes.....	2,106	1,647	4,46
Pro forma net earnings.....	\$ 18,079	\$ 19,818	\$ 40,31
Basic net earnings per common share, as reported.....	\$ 0.36	\$ 0.38	\$ 0.8
Basic net earnings per common share, pro forma.....	\$ 0.33	\$ 0.35	\$ 0.7
Diluted net earnings per common share, as reported.....	\$ 0.35	\$ 0.37	\$ 0.7
Diluted net earnings per common share, pro forma.....	\$ 0.32	\$ 0.35	\$ 0.7

3. Commitments and Contingencies

Litigation, claims and disputes: We are involved in various legal actions which include, without limitation, employment law related matters, dram shop claims, personal injury claims and other such normal restaurant operational matters. In each instance, we believe that we have meritorious defenses to the allegations made and we are vigorously defending these claims.

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

Lease guarantees: 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 June 29, 2003, the aggregate amount of these lease payments totaled approximately \$23,700,000. These leases expire at various times throughout the next several years with the final lease agreement expiring in 2018. The buyers have indemnified us from any losses related to these guarantees. We have not recorded a liability as of June 29, 2003 or December 29, 2002.

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 June 29, 2003, we would have been required to make payments totaling approximately \$10,000,000. 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 \$5,800,000 if such officers had been terminated as of June 29, 2003.

4. Earnings Per Share

We compute basic earnings per share by dividing income available to common

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

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 and equity-based compensation 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		26
	June 29, 2003	June 30, 2002	June 29 2003
Net earnings.....	\$ 20,185	\$ 21,465	\$ 44,78
Basic weighted average shares outstanding.....	55,435	55,872	55,35
Dilutive effect of stock options and equity-based compensation.....	1,597	1,502	1,51
Diluted weighted average shares outstanding.....	57,032	57,374	56,86
Basic net earnings per common share.....	\$ 0.36	\$ 0.38	\$ 0.8
Diluted net earnings per common share.....	\$ 0.35	\$ 0.37	\$ 0.7

5. Acquisitions

On November 7, 2002, we acquired the operations and assets of 21 Applebee's restaurants located in the Washington, D.C. area from a franchisee. Under the terms of the purchase agreement and the agreement with the franchisee's secured lender, the total purchase price of the acquisition was \$34,250,000. The agreement also provides for additional consideration in July 2004 if the restaurants achieve cash flows in excess of historical levels. Our financial statements reflect the results of operations for these restaurants subsequent to the date of acquisition. The purchase price of \$34,250,000 has been allocated to the fair value of property and equipment of \$25,200,000, goodwill of \$10,100,000 and other net current liabilities of \$1,050,000.

On March 24, 2003, we acquired the operations and assets of 11 Applebee's restaurants located in Illinois, Indiana, Kentucky and Missouri for \$21,800,000 in cash and \$1,400,000 in assumed debt from a franchisee. The total cash payment included \$20,800,000 paid at closing, approximately \$200,000 paid as a deposit in fiscal 2002 and approximately \$800,000 paid in the second quarter of 2003. Our financial statements reflect the results of operations for these restaurants subsequent to the date of acquisition. The purchase price of \$23,200,000 has been allocated to the fair value of property and equipment of \$7,900,000, goodwill of \$16,600,000, and other net liabilities of \$1,300,000.

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

The following table is comprised of actual company restaurant sales included in our consolidated financial statements for each period presented and pro forma company restaurant sales assuming the acquisitions occurred at the beginning of each respective period (in thousands):

	13 Weeks Ended		26
	June 29, 2003	June 30, 2002	June 29 2003
Actual company restaurant sales.....	\$ 18,700	\$ --	\$ 30,70
Pro forma company restaurant sales.....	\$ 18,700	\$ 17,100	\$ 36,70

6. Impairment of Chevys Note Receivable

In 1999, we received a \$6,000,000, 8% subordinated note in connection with the sale of the Rio Bravo concept to Chevys Holdings, Inc ("Chevys") due in 2009. The note receivable balance of approximately \$8,800,000 and \$8,600,000 as of June 29, 2003 and December 29, 2002, respectively, is included in other assets in our consolidated balance sheets. In June 2003, Chevys announced the sale of the majority of its restaurants. Subsequent to the announcement, we received Chevys' audited financial statements for the fiscal year ended December 31, 2002. Based upon this information, we believe that the note is impaired. We have fully reserved the principal and accrued interest by recording an allowance of approximately \$8,800,000 as of June 29, 2003. A charge for the impairment of this note is included in our consolidated statements of earnings. We will no longer accrue interest receivable on this note and will record future interest income on this note only upon the receipt of any related cash payments.

7. Goodwill and Other Intangible Assets

Changes in goodwill are summarized below (in thousands):

	June 29, 2003	December 29 2002
Carrying amount, beginning of the year.....	\$ 88,715	\$ 78,61
Goodwill acquired during the period.....	16,611	10,10
	\$ 105,326	\$ 88,71

Intangible assets subject to amortization pursuant to SFAS No. 142, "Goodwill and Other Intangible Assets," consist of franchise interest and rights and are summarized below (in thousands):

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

	June 29, 2003	December 29 2002
Gross carrying amount.....	\$ 6,371	\$ 6,371
Less, accumulated amortization.....	5,069	4,900
Net.....	\$ 1,302	\$ 1,466

We expect annual amortization expense for all intangible assets for the next five fiscal years to range from approximately \$280,000 to \$380,000.

11

8. Captive Insurance Subsidiary

On September 20, 2002, we formed Neighborhood Insurance, Inc., a Vermont corporation and a wholly-owned subsidiary, as a captive insurance company. Neighborhood Insurance, Inc. was established to provide Applebee's International, Inc. and qualified franchisees with workers' compensation and general liability insurance. Applebee's International, Inc. and covered franchisees make premium payments to the captive insurance company which pays administrative fees and insurance claims, subject to individual and aggregate maximum claim limits under the captive insurance company's reinsurance policies. Franchisee premium amounts billed by the captive insurance company were established based upon third-party actuarial estimates of ultimate settlement costs for incurred claims and administrative fees. The franchisee premiums are included in other franchise income ratably over the policy year. The related offsetting expenses are included in cost of other franchise income. Accordingly, we do not expect franchisee participation in the captive insurance company to have an impact on our net earnings.

As of June 29, 2003 we have included approximately \$2,000,000 in deferred policy acquisition costs in prepaid and other current assets and approximately \$1,600,000 of investments in other assets in our consolidated balance sheet related to the captive insurance company.

9. New Accounting Pronouncements

In June 2002, the Financial Accounting Standards Board ("FASB") issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." This Statement requires that a liability for a cost associated with an exit or disposal activity be recognized only when the liability is incurred and measured at fair value. SFAS No. 146 is effective for exit or disposal activities that are initiated after December 31, 2002. The initial adoption of this Statement did not have a material impact on our results of operations or financial position.

In November 2002, the FASB issued Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, including Indirect Guarantees of Indebtedness of Others." Interpretation No. 45 supersedes Interpretation No. 34, "Disclosure of Indirect Guarantees of Indebtedness of Others," and provides guidance to guarantors on the recognition and disclosure concerning obligations under certain guarantees in interim and annual financial statements. The initial recognition and measurement provisions of Interpretation No. 45 are effective for guarantees issued or modified after December 31, 2002, and are to be applied prospectively. The disclosure requirements were effective for financial statements for interim or annual periods ending after December 15, 2002. We

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

adopted the initial recognition provisions of Interpretation No. 45 in January of 2003. The initial adoption of Interpretation No. 45 did not have a material impact on our results of operations or financial position.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure." SFAS No. 148 amends SFAS No. 123, "Accounting for Stock-Based Compensation," and provides alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. This Statement also amends the disclosure requirements of SFAS No. 123 to require prominent disclosure in annual and interim financial statements about the effects of stock-based compensation. The transition guidance and annual disclosure provisions of SFAS No. 148 are effective for financial statements issued for fiscal years ending after December 15, 2002. The interim disclosure provisions of this Statement were effective for financial reports containing financial statements for interim periods beginning after December 15, 2002. We have adopted the disclosure provisions of SFAS No. 148.

12

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51." This Interpretation provides clarification on the consolidation of certain entities in which equity investors do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. Such entities are defined as variable interest entities ("VIEs"). This Interpretation requires that VIEs be consolidated by the entity considered to be the primary beneficiary of the VIE. The Interpretation is effective for newly created VIEs after January 31, 2003 and effective in the second quarter 2003 for any VIEs created prior to February 1, 2003. We have evaluated our relationships with potential unconsolidated entities which may meet the consolidation requirements of this Interpretation, and the initial adoption did not have any impact on our consolidated financial statements.

10. Subsequent Event

On July 20, 2003, we completed the sale of eight company restaurants in the Atlanta, Georgia market to an affiliate of an existing franchisee for \$8,000,000. We do not expect this transaction to have a significant impact on our net earnings for fiscal 2003, and no significant gain or loss on the sale is anticipated. Actual company restaurant sales included in our consolidated financial statements for these restaurants were approximately \$4,300,000 in both the 13 weeks ended June 29, 2003 and June 30, 2002 and were approximately \$8,800,000 in both the 26 weeks ended June 29, 2003 and June 30, 2002. In connection with this sale, we closed one restaurant in the Atlanta market in June 2003.

13

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

General

Our revenues are generated from three primary sources:

- o Company restaurant sales (food and beverage sales)
- o Franchise royalties and fees

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

o Other franchise income

Beverage sales include sales of alcoholic beverages, while non-alcoholic beverages are included in food sales. Franchise royalties are generally 4% of each franchise restaurant's monthly gross sales. Franchise fees typically range from \$30,000 to \$35,000 for each restaurant opened. Other franchise income includes insurance premiums from franchisee participation in our captive insurance company and revenue from information technology products and services provided to certain franchisees.

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

Cost of other franchise income includes the costs related to franchisee participation in our captive insurance company and costs related to information technology products and services provided to certain franchisees.

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 June 29, 2003 and June 30, 2002 each contained 13 weeks and are referred to hereafter as the "2003 quarter" and the "2002 quarter," respectively. Our 26 week periods ended June 29, 2003 and June 30, 2002 are referred to hereafter as the "2003 year-to-date period" and the "2002 year-to-date period," respectively.

On September 20, 2002, we formed Neighborhood Insurance, Inc., a Vermont corporation and a wholly-owned subsidiary, as a captive insurance company. Neighborhood Insurance, Inc. was established to provide Applebee's International, Inc. and qualified franchisees with workers' compensation and general liability insurance. Applebee's International, Inc. and covered franchisees make premium payments to the captive insurance company which pays administrative fees and insurance claims, subject to individual and aggregate maximum claim limits under the captive insurance company's reinsurance policies. Franchisee premium amounts billed by the captive insurance company were established based upon third-party actuarial estimates of ultimate settlement costs for incurred claims and administrative fees. The franchisee premiums are included in other franchise income ratably over the policy year. The related offsetting expenses are included in cost of other franchise income. Accordingly, we do not expect franchisee participation in the captive insurance company to have an impact on our net earnings.

14

As of June 29, 2003 we have included approximately \$2,000,000 in deferred policy acquisition costs in prepaid and other current assets and approximately \$1,600,000 of investments in other assets in our consolidated balance sheet related to the captive insurance company.

Application of Critical Accounting Policies

Management's Discussion and Analysis of Financial Condition and Results of Operations is based upon our consolidated financial statements, which were prepared in accordance with accounting principles generally accepted in the United States of America. These principles require us to make estimates and assumptions that affect the reported amounts in the consolidated financial

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

statements and notes thereto. Actual results may differ from these estimates, and such differences may be material to the consolidated financial statements. We believe that the following significant accounting policies involve a higher degree of judgement or complexity (see Note 2 of our Consolidated Financial Statements in our Annual Report on Form 10-K for the fiscal year ended December 29, 2002 for a complete discussion of our significant accounting policies).

Franchise revenues: Franchise revenues consist of franchise royalties, franchise fees and other franchise income. We recognize royalties on a franchisee's sales in the period in which the sales occur. We also receive a franchise fee for each restaurant that a franchisee opens. Franchise fees are deferred until we have performed substantially all of our related obligations as franchisor, typically when the restaurant opens. Other franchise income includes insurance premiums from franchisee participation in our captive insurance company and revenue from information technology products and services provided to certain franchisees.

Property and equipment: Property and equipment are depreciated on a straight-line basis over the estimated useful lives of the assets. The useful lives of the assets are based upon management's expectations. We periodically review the assets for changes in circumstances which may impact their useful lives.

Impairment of long-lived assets: We periodically review property and equipment for impairment using historical cash flows as well as current estimates of future cash flows and/or appraisals. This assessment process requires the use of estimates and assumptions which are subject to a significant degree of judgement. In addition, we periodically assess the recoverability of goodwill and other intangible assets, which requires us to make assumptions regarding the future cash flows and other factors to determine the fair value of the assets. If these assumptions change in the future, we may be required to record impairment charges for these assets.

Legal and insurance reserves: We are periodically involved in various legal actions. We are required to assess the probability of any adverse judgments as well as the potential range of loss. We determine the required accruals after a review of the facts of each legal action.

We use estimates in the determination of the appropriate liabilities for general liability, workers' compensation and health insurance. The estimated liability is established based upon historical claims data and third-party actuarial estimates of settlement costs for incurred claims. Unanticipated changes in these factors may require us to revise our estimates.

Employee incentive compensation plans: We have various long-term employee incentive compensation plans which require us to make estimates to determine our liability based upon projected performance of plan criteria. If actual performance against the criteria differs from our estimates in the future, we will be required to adjust our liability accordingly.

15

Receivables: We continually assess the collectibility of our franchise receivables. We establish our allowance for bad debts based on several factors, including historical collection experience, the current economic environment and other specific information available to us at the time. The allowance for bad debts may change in the future due to changes in the factors above or other new developments.

We periodically reassess our assumptions and judgements and make adjustments when significant facts and circumstances dictate. A change in any of the above estimates could impact our consolidated statements of earnings and the related

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

asset or liability recorded in the consolidated balance sheets would be adjusted accordingly. Historically, actual results have not been materially different than the estimates that are described above.

Acquisitions

On November 7, 2002, we acquired the operations and assets of 21 Applebee's restaurants located in the Washington, D.C. area from a franchisee. Under the terms of the purchase agreement and the agreement with the franchisee's secured lender, the total purchase price of the acquisition was \$34,250,000. The agreement also provides for additional consideration in July 2004 if the restaurants achieve cash flows in excess of historical levels. Our financial statements reflect the results of operations for these restaurants subsequent to the date of acquisition.

On March 24, 2003, we acquired the operations and assets of 11 Applebee's restaurants located in Illinois, Indiana, Kentucky and Missouri for \$21,800,000 in cash and \$1,400,000 in assumed debt from a franchisee. The total cash payment included \$20,800,000 paid at closing, approximately \$200,000 paid as a deposit in fiscal 2002 and approximately \$800,000 paid in the second quarter of 2003. Our financial statements reflect the results of operations for these restaurants subsequent to the date of acquisition.

The following table is comprised of actual company restaurant sales included in our consolidated financial statements for each period presented and pro forma company restaurant sales assuming the acquisitions occurred at the beginning of each respective period (in thousands):

	13 Weeks Ended		26
	June 29, 2003	June 30, 2002	June 29 2003
Actual company restaurant sales.....	\$ 18,700	\$ --	\$ 30,700
Pro forma company restaurant sales.....	\$ 18,700	\$ 17,100	\$ 36,700

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 Ended		26
	June 29,	June 30,	June

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

	2003	2002	2001
	-----	-----	-----
Revenues:			
Company restaurant sales.....	87.8%	87.3%	87.3%
Franchise royalties and fees.....	10.9	12.4	11.1
Other franchise income.....	1.3	0.2	1.1
	-----	-----	-----
Total operating revenues.....	100.0%	100.0%	100.0%
	=====	=====	=====
Cost of sales (as a percentage of company restaurant sales):			
Food and beverage.....	25.9%	26.3%	26.3%
Labor.....	32.6	32.9	32.9
Direct and occupancy.....	24.7	24.8	24.8
Pre-opening expense.....	0.2	0.2	0.2
	-----	-----	-----
Total cost of sales.....	83.4%	84.2%	83.4%
	=====	=====	=====
Cost of other franchise income (as a percentage of other franchise income):			
General and administrative expenses.....	97.1%	20.1%	96.5%
Amortization of intangible assets.....	9.1	9.7	9.7
Loss on disposition of restaurants and equipment.....	--	--	--
	-----	-----	-----
Operating earnings.....	0.3	0.4	0.4
	-----	-----	-----
Operating earnings.....	16.1	16.4	16.4
	-----	-----	-----
Other income (expense):			
Investment income.....	0.2	0.2	0.2
Interest expense.....	(0.2)	(0.3)	(0.3)
Impairment of Chevys note receivable.....	(3.5)	--	(1.1)
Other income.....	--	0.2	--
	-----	-----	-----
Total other income (expense).....	(3.5)	0.2	(1.1)
	-----	-----	-----
Earnings before income taxes.....	12.5	16.5	14.9
Income taxes.....	4.5	6.0	5.5
	-----	-----	-----
Net earnings.....	8.1%	10.5%	9.4%
	=====	=====	=====

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 Ended		
	June 29, 2003	June 30, 2002	June 29, 2001
	-----	-----	-----
Number of restaurants:			
Company:			
Beginning of period.....	371	314	287

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

Restaurant openings.....	4	4	
Restaurants closed.....	(2)	--	
Restaurants acquired from franchisee.....	--	--	
	-----	-----	-----
End of period.....	373	318	
	-----	-----	-----
Franchise:			
Beginning of period.....	1,142	1,090	
Restaurant openings.....	13	15	
Restaurants closed.....	--	(2)	
Restaurants acquired from franchisee.....	--	--	
	-----	-----	-----
End of period.....	1,155	1,103	
	-----	-----	-----
Total:			
Beginning of period.....	1,513	1,404	
Restaurant openings.....	17	19	
Restaurants closed.....	(2)	(2)	
	-----	-----	-----
End of period.....	1,528	1,421	
	=====	=====	=====
Weighted average weekly sales per restaurant:			
Company.....	\$ 45,402	\$ 43,558	\$
Franchise.....	\$ 45,940	\$ 44,566	\$
Total.....	\$ 45,807	\$ 44,340	\$
Change in comparable restaurant sales: (1)			
Company.....	5.1%	1.4%	
Franchise.....	3.2%	3.7%	
Total.....	3.6%	3.2%	
Total system sales (in thousands).....	\$ 904,238	\$ 812,707	\$ 1,7

(1) When computing comparable restaurant sales, restaurants open for at least 18 months are compared from period to period.

Company Restaurant Sales. Total company restaurant sales increased \$41,214,000 (23%) from \$178,893,000 in the 2002 quarter to \$220,107,000 in the 2003 quarter and increased \$74,651,000 (21%) from \$353,866,000 in the 2002 year-to-date period to \$428,517,000 in the 2003 year-to-date period. Company restaurant openings contributed approximately 8% of the increase in total company

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

restaurant sales in both the 2003 quarter and the 2003 year-to-date period. The remaining increase in both periods was due to the acquisition of 21 franchise restaurants in the Washington, D.C. area in November 2002 and 11 restaurants in Illinois, Indiana, Kentucky, and Missouri in late March 2003 as well as increases in weighted average weekly sales.

Comparable restaurant sales at company restaurants increased by 5.1% and 4.9% in the 2003 quarter and the 2003 year-to-date period, respectively. Weighted average weekly sales at company restaurants increased 4.2% from \$43,558 in the 2002 quarter to \$45,402 in the 2003 quarter and increased 3.8% from \$43,398 in the 2002 year-to-date period to \$45,041 in the 2003 year-to-date period. These increases were due primarily to increases in guest traffic and in the average guest check resulting from our food promotions. In addition, a portion of the increase resulted from the implementation of our To Go initiative and menu price increases of approximately 1.5% in fiscal 2003. To Go sales mix increased from 4.6% of company restaurant sales in the 2002 quarter to 6.8% of company restaurant sales in the 2003 quarter.

Franchise Royalties and Fees. Overall franchise income increased \$1,847,000 (7%) from \$25,484,000 in the 2002 quarter to \$27,331,000 in the 2003 quarter and increased \$4,170,000 (8%) from \$50,324,000 in the 2002 year-to-date period to \$54,494,000 in the 2003 year-to-date period. These increases were due primarily to the increased number of franchise restaurants operating during the 2003 quarter and 2003 year-to-date period and increases in comparable restaurant sales. Weighted average weekly sales at franchise restaurants increased 3.1% in both the 2003 quarter and 2003 year-to-date period, respectively, and franchise comparable restaurant sales increased 3.2% and 3.0% in the 2003 quarter and 2003 year-to-date period, respectively.

Other Franchise Income. Other franchise income increased from \$463,000 in the 2002 quarter to \$3,268,000 in the 2003 quarter and increased from \$597,000 in the 2002 year-to-date period to \$5,909,000 in the 2003 year-to-date period due primarily to revenues recognized related to the franchise premium amounts billed by the captive insurance company which was formed in September 2002. Franchise premiums are included in other franchise income ratably over the policy year.

Cost of Company Restaurant Sales. Food and beverage costs decreased from 26.3% in the 2002 quarter to 25.9% in the 2003 quarter and decreased from 26.7% in the 2002 year-to-date period to 26.1% in the 2003 year-to-date period. The decreases in both the 2003 quarter and 2003 year-to-date period were due to menu price increases and operational improvements resulting from our supply chain management initiatives. The decrease in the 2003 year-to-date period was also due to lower beef usage related to our menu promotions.

Labor costs decreased from 32.9% in both the 2002 quarter and the 2002 year-to-date period to 32.6% in the 2003 quarter and 32.7% in the 2003 year-to-date period. These decreases were due to lower hourly and management costs due to higher sales volumes at company restaurants, lower staffing levels and lower incentive compensation which were partially offset by higher workers' compensation costs.

19

Direct and occupancy costs decreased from 24.8% in the 2002 quarter and 24.6% in the 2002 year-to-date period to 24.7% in the 2003 quarter and 24.5% in the 2003 year-to-date period. Higher sales volumes at company restaurants during the 2003 quarter and the 2003 year-to-date period resulted in lower depreciation expense, as a percentage of sales, due to its relatively fixed nature. Decreases in both periods were partially offset by higher packaging costs relating to our To Go initiative. Advertising costs, as a percentage of sales, were higher in the 2003 quarter but lower in the 2003 year-to-date period due to the timing of our menu

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

promotions.

Cost of Other Franchise Income. Cost of other franchise income increased from \$93,000 in the 2002 quarter to \$3,173,000 in the 2003 quarter and increased from \$153,000 in the 2002 year-to-date period to \$5,673,000 in the 2003 year-to-date due primarily to the costs related to the operation of our captive insurance company, which was formed in September 2002.

General and Administrative Expenses. General and administrative expenses decreased from 9.7% in both the 2002 quarter and the 2002 year-to-date period to 9.1% in the 2003 quarter and 9.3% in the 2003 year-to-date period. General and administrative expenses were lower in both the 2003 quarter and 2003 year-to-date period due to the absorption of general and administrative expenses over a larger revenue base and a reduction in bad debt expense. Decreases in both periods were partially offset by higher depreciation expense related to our new information systems and increased compensation due to staffing levels.

Impairment of Chevys Note Receivable. In June 2003, Chevys announced the sale of the majority of its restaurants. Subsequent to the announcement, we received Chevys' audited financial statements for the fiscal year ended December 31, 2002. Based upon this information, we believe that the note is impaired. We have fully reserved the principal and accrued interest by recording an allowance of approximately \$8,800,000 as of June 29, 2003.

Income Taxes. The effective income tax rate, as a percentage of earnings before income taxes, decreased from 36.5% in both the 2002 quarter and 2002 year-to-date period to 35.8% in the 2003 quarter and 36.0% in the 2003 year-to-date period due to a reduction in state and local income taxes and the discontinuation of goodwill amortization required under SFAS No. 142.

Liquidity and Capital Resources

Our need for capital historically has resulted from the construction and acquisition of restaurants, investment in information technology systems and the repurchase of our common shares. In the past, we have obtained capital through public stock offerings, debt financing, and our ongoing operations. Cash flows from our ongoing operations include 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 \$64,874,000 in fiscal year 2002 (excluding the acquisition of 21 restaurants) and \$28,964,000 in the 2003 year-to-date period (excluding the acquisition of 11 restaurants). We currently expect to open approximately 25 company restaurants, and capital expenditures excluding acquisitions are expected to be between \$70,000,000 and \$80,000,000 in 2003. These expenditures will primarily be for the development of new 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.

On November 7, 2002, we acquired the operations and assets of 21 Applebee's

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

restaurants located in the Washington, D.C. area from a franchisee. Under the terms of the purchase agreement and the agreement with the franchisee's secured lender, the total purchase price of the acquisition was \$34,250,000. The agreement also provides for additional consideration in July 2004 if the restaurants achieve cash flows in excess of historical levels. Our financial statements reflect the results of operations for these restaurants subsequent to the date of acquisition.

On March 24, 2003, we acquired the operations and assets of 11 Applebee's restaurants located in Illinois, Indiana, Kentucky and Missouri for \$21,800,000 in cash and \$1,400,000 in assumed debt from a franchisee. The total cash payment included \$20,800,000 paid at closing, approximately \$200,000 paid as a deposit in fiscal 2002 and approximately \$800,000 paid in the second quarter of 2003. Our financial statements reflect the results of operations for these restaurants subsequent to the date of acquisition.

Our bank credit agreement provides for a \$150,000,000 three-year unsecured revolving credit facility, of which \$25,000,000 may be used for the issuance of letters of credit. The facility is subject to various covenants and restrictions which, among other things, require the maintenance of stipulated fixed charge, leverage and indebtedness to capitalization ratios, as defined, and limit additional indebtedness and capital expenditures in excess of specified amounts. Cash dividends are limited to \$10,000,000 annually. The facility is subject to standard other terms, conditions, covenants, and fees. We are currently in compliance with the covenants contained in our credit agreement. As of June 29, 2003, we had borrowings of \$29,000,000 and standby letters of credit of \$11,939,000 outstanding under our revolving credit facility.

In May 2002, our Board of Directors authorized an additional repurchase of \$75,000,000 of our common stock through May 2005. During the 2003 year-to-date period, we repurchased 545,000 shares at an average cost of \$24.37 for an aggregate cost of \$13,300,000. As of June 29, 2003, we had \$56,200,000 remaining under the 2002 authorization.

As of June 29, 2003, our liquid assets totaled \$4,561,000. These assets consisted of cash and cash equivalents in the amount of \$4,535,000 and short-term investments in the amount of \$26,000. The working capital deficit decreased from \$45,607,000 as of December 29, 2002 to \$40,741,000 as of June 29, 2003. This decrease was due primarily to the redemption of gift certificates in the 2003 year-to-date period sold in 2002 and an increase in inventory and were partially offset by decreases in cash and cash equivalents due to the acquisition of 11 restaurants in Illinois, Indiana, Kentucky and Missouri, repurchases of our common stock and the repayment of debt.

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.

21

The following table shows our debt amortization schedule, our future capital lease commitments (including principal and interest payments) and our future operating lease commitments as of June 29, 2003 (in thousands):

Payments due by period

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

Certain Contractual Obligations	Total	Less than 1 year	1-3 years	3-5 years
Long-term Debt (excluding capital lease obligations).....	\$ 31,024	\$ 441	\$ 29,236	\$ 1,347
Capital Lease Obligations.....	\$ 10,186	\$ 729	\$ 1,534	\$ 7,923
Operating Leases.....	\$ 215,630	\$ 18,550	\$ 34,642	\$ 33,438

In addition, we have outstanding lease guarantees of approximately \$23,700,000 as of June 29, 2003 (see Note 3 to our Consolidated Financial Statements).

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 considering 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.

New Accounting Pronouncements

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." This Statement requires that a liability for a cost associated with an exit or disposal activity be recognized only when the liability is incurred and measured at fair value. SFAS No. 146 is effective for exit or disposal activities that are initiated after December 31, 2002. The initial adoption of this Statement did not have a material impact on our results of operations or financial position.

In November 2002, the FASB issued Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, including Indirect Guarantees of Indebtedness of Others." Interpretation No. 45 supersedes Interpretation No. 34, "Disclosure of Indirect Guarantees of Indebtedness of Others," and provides guidance to guarantors on the recognition and disclosure concerning obligations under certain guarantees in interim and annual financial statements. The initial recognition and measurement provisions of Interpretation No. 45 are effective for guarantees issued or modified after December 31, 2002, and are to be applied prospectively. The disclosure requirements were effective for financial statements for interim or annual periods ending after December 15, 2002. We adopted the initial recognition provisions of Interpretation No. 45 in January of 2003. The initial adoption of Interpretation No. 45 did not have a material impact on our results of operations or financial position.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

Compensation - Transition and Disclosure." SFAS No. 148 amends SFAS No. 123, "Accounting for Stock-Based Compensation," and provides alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. This Statement also amends the disclosure requirements of SFAS No. 123 to require prominent disclosure in annual and interim financial statements about the effects of stock-based compensation. The transition guidance and annual disclosure provisions of SFAS No. 148 are effective for financial statements issued for fiscal years ending after December 15, 2002. The interim disclosure provisions of this Statement were effective for financial reports containing financial statements for interim periods beginning after December 15, 2002. We have adopted the disclosure provisions of SFAS No. 148.

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51." This Interpretation provides clarification on the consolidation of certain entities in which equity investors do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. Such entities are defined as variable interest entities ("VIEs"). This Interpretation requires that VIEs be consolidated by the entity considered to be the primary beneficiary of the VIE. The Interpretation is effective for newly created VIEs after January 31, 2003 and effective in the second quarter 2003 for any VIEs created prior to February 1, 2003. We have evaluated our relationships with potential unconsolidated entities which may meet the consolidation requirements of this Interpretation, and we do not believe the adoption will have a material impact on our consolidated financial statements.

Forward-Looking Statements

The statements contained in the "Management's Discussion and Analysis of Financial Condition and Results of Operations" section regarding restaurant development, capital expenditures and financial commitments 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 our ability and the ability of our franchisees to open and operate additional restaurants profitably, the ability of our franchisees to obtain financing, the continued growth of our franchisees, our ability to attract and retain qualified franchisees, 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 12, 2003. We disclaim any obligation to update forward-looking statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to market risk from fluctuations in interest rates and changes in commodity prices. Our revolving credit facility bears interest at either the bank's prime rate or LIBOR plus 1.0%, at our option. As of June 29, 2003, the total amount of debt subject to interest rate fluctuations was \$29,000,000 which was outstanding on our revolving credit facility. A 1% change in interest rates would result in an increase or decrease in interest expense of \$290,000 per year. We may from time to time enter into interest rate swap agreements to manage the impact of interest rate changes on our earnings. Many of the food products we purchase are subject to price volatility due to factors that are outside of our control such as weather and seasonality. As part of our strategy to moderate this volatility, we have entered into fixed price purchase commitments.

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

Item 4. Controls and Procedures

As of the end of the period covered by this report, we have evaluated the effectiveness of the design and operation of our disclosure controls and procedures under the supervision and with the participation of the Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"). Based on this evaluation, our management, including the CEO and CFO, concluded that our disclosure controls and procedures were effective. There have been no significant changes in our internal controls or in other factors that could significantly affect internal controls subsequent to the date of their evaluation.

24

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We are involved in various legal actions which include, without limitation, employment law related matters, dram shop claims, personal injury claims and other such normal restaurant operational matters. In each instance, we believe that we have meritorious defenses to the allegations made and we are vigorously defending these claims.

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

Item 4. Submission of Matters to a Vote of Security Holders

Our annual meeting of stockholders was held on May 8, 2003. The stockholders voted on the following matters:

- Proposal I. Elect Douglas R. Conant and D. Patrick Curran as directors to serve three-year terms expiring in 2006.
- Proposal II. Approve an amendment to the Applebee's International, Inc. 1995 Equity Incentive Plan.
- Proposal III. Approve an amendment to the Applebee's International, Inc. Certificate of Incorporation.
- Proposal IV. Ratify Deloitte & Touche LLP as our independent auditors for the 2003 fiscal year.
- Proposal V. Act on a Shareholder Proposal to require us to issue a report relating to genetically engineered ingredients.

The results of the voting were as follows:

Proposal	Affirmative Votes	Negative Votes	Abstentions
----------	----------------------	-------------------	-------------

Edgar Filing: APPLEBEES INTERNATIONAL INC - Form 10-Q

I (Conant)	49,924,641	1,552,887	--
I (Curran)	37,393,989	14,083,539	--
II	34,979,717	16,294,398	77,672
III	11,662,859	32,767,059	73,208
IV	32,892,023	18,425,756	34,008
V	2,740,750	40,200,587	1,521,783

Proposals I, II and IV received the required affirmative votes and were affirmatively adopted by the Stockholders. Proposals III and V did not receive the required affirmative votes.

25

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 furnished a report on Form 8-K on April 3, 2003 announcing our presentation at the SunTrust Robinson Humphrey Institutional Investor Conference.

We filed a report on Form 8-K on April 8, 2003 announcing the sale of eight restaurants in the Atlanta market to a franchisee.

We furnished a report on Form 8-K on April 24, 2003 announcing the webcast of our first quarter earnings conference call over the Internet.

We furnished a report on Form 8-K on May 1, 2003 reporting first quarter diluted earnings per share.

We filed a report on Form 8-K on May 22, 2003 announcing the establishment of a plan to manage the exercise and sale of certain stock options by our Chairman and Chief Executive Officer.

We filed a report on Form 8-K on May 28, 2003 reporting May comparable sales.

We furnished a report on Form 8-K on May 29, 2003 announcing our presentation at the Goldman Sachs Lodging, Gaming, Restaurants, and Leisure Conference.

We furnished a report on Form 8-K on June 6, 2003 announcing our presentation at two Investment Conferences in June.

26

SIGNATURES

Edgar Filing: APPLEBEE'S INTERNATIONAL INC - Form 10-Q

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: July 30, 2003

By: /s/ Lloyd L. Hill

Lloyd L. Hill
Chairman and Chief Executive Officer
(principal executive officer)

Date: July 30, 2003

By: /s/ Steven K. Lumpkin

Steven K. Lumpkin
Executive Vice President and
Chief Financial Officer
(principal financial officer)

Date: July 30, 2003

By: /s/ Beverly O. Elving

Beverly O. Elving
Vice President, Accounting
(principal accounting officer)

27

APPLEBEE'S INTERNATIONAL, INC.
EXHIBIT INDEX

Exhibit Number	Description of Exhibit
99.1	Certification of Chairman and Chief Executive Officer Pursuant to SEC Rule 13a-14
99.2	Certification of Chief Financial Officer Pursuant to SEC Rule 13a-14
99.3	Certification of Chairman and Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350

28