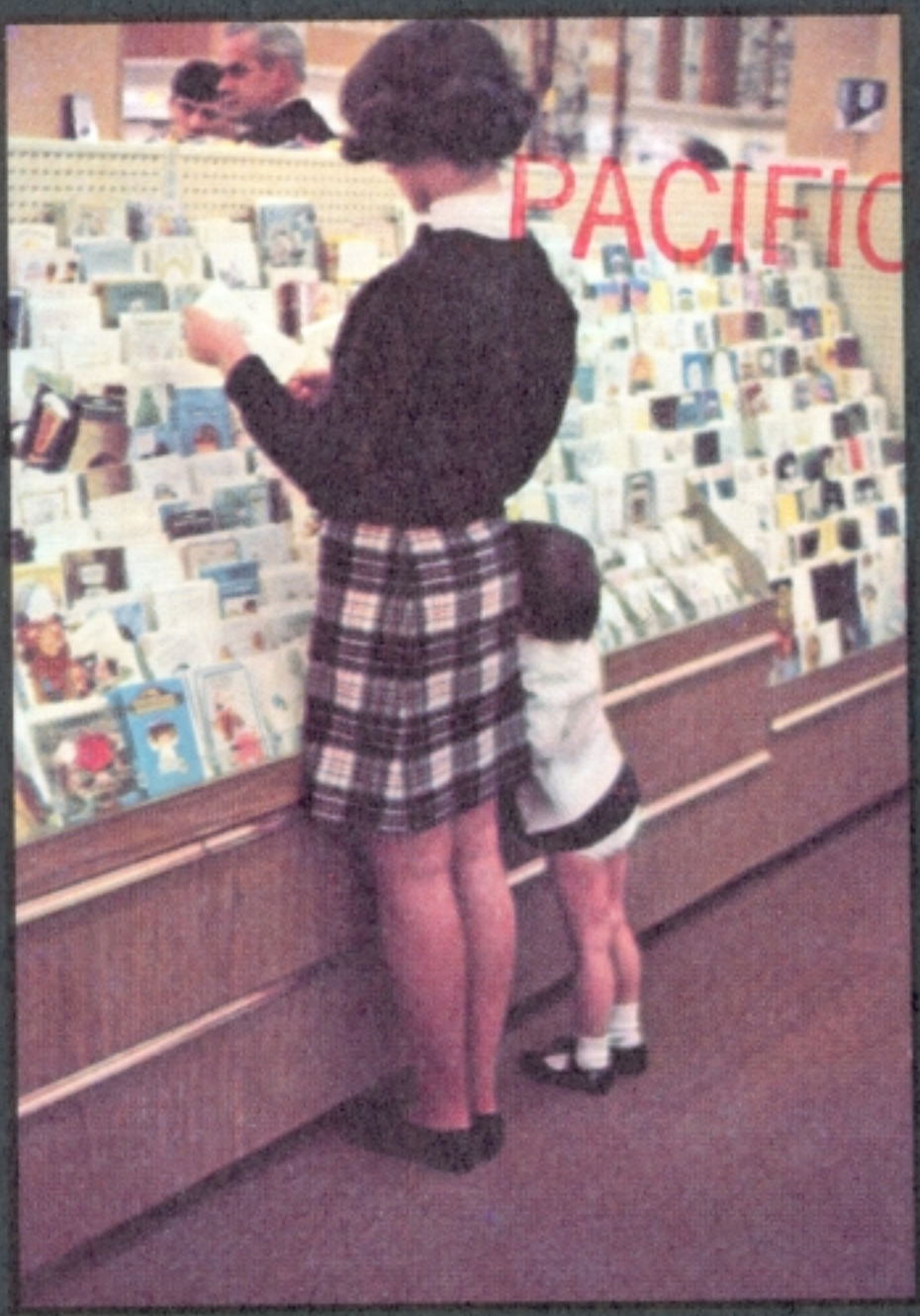
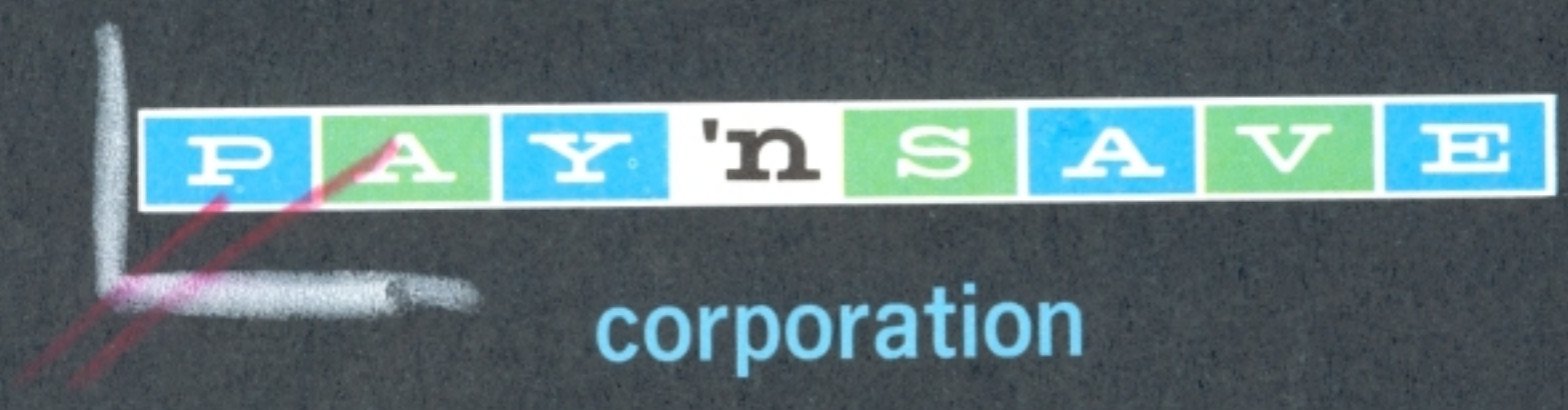


SEATTLE PUBLIC LIBRARY
Business & Economics
REFERENCE COPY

ANNUAL REPORTS
PAY'n SAVE Corp. 1968
Foster Business Library
University of Washington



annual report for the year ending january 31, 1968

Financial Highlights

	<i>Year Ended — January 31,</i> <u>1968</u>	<u>1967</u>	<u>Increase</u>
Sales	\$57,573,851	\$41,671,839	\$15,902,012
Net Income	\$ 1,900,341	\$ 1,230,123	\$ 670,218
Net Income per Average Shares Outstanding....	\$3.53	\$2.45	\$1.08

To the Stockholders

The year ended, January 31, 1968 was the most successful in your company's history. New records were established in sales and net income. Also, net income as a percentage of sales was the highest ever. We entered a new marketing area with the opening of a Pay'n Save Drug Store in Anchorage, Alaska and we entered into a complete new merchandising field with the acquisition of the four store chain of Rhodes Department Stores of Seattle on November 1, 1967.

Sales up 38%

Annual sales for the first time exceeded fifty million dollars, amounting to \$57,573,851 (including \$2,187,000 of Rhodes Department Store sales since acquisition November 1, 1967.) This is an increase of \$15,902,012 or 38%. In the face of substantial new competition, national companies moving into our marketing area, we were able to continue our fine sales growth pattern. The strong economy of the Puget Sound area, additional store openings during the year, and an aggressive advertising program contributed to this pleasing sales record.

Net Income up 54%

Again this year, net income increased more rapidly than sales. Net of \$1,900,341 (including \$32,311 from Rhodes since acquisition) or \$3.53 per



M. L. BEAN
Chairman of the Board



M. LAMONT BEAN
President and Director



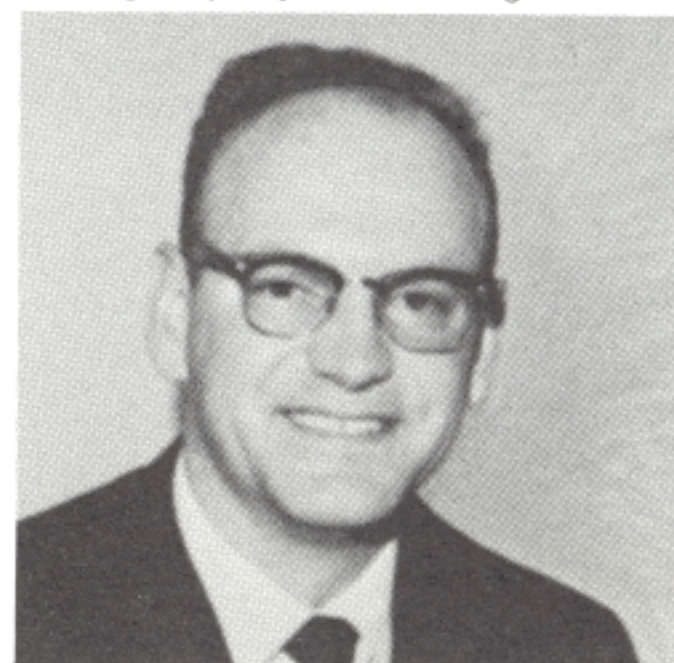
JOSHUA GREEN JR.
Director



H. E. ONEAL
*Vice President, Director and General
Manager of Pay'n Save Drug Division*



JAMES H. CLAWSON
Director



CALVIN HENDRICKS
Treasurer and Controller



E. R. ERICKSON
*Vice President, Director and General
Manager of Ernst Hardware Division*

share on the average shares outstanding was 54% above the net income of \$1,230,123 or \$2.45 per share for the preceding year. The strengthening and maturing of stores opened in recent years, plus heavy emphasis on store efficiency and cost controls added greatly to the profits.

Rhodes Acquisition

On November 1, your company acquired the Rhodes of Seattle Department Stores with operations in downtown Seattle, Crossroads, University Village and Lake Forest Park. Each of these stores, except the downtown store, is located in a suburban shopping area near Seattle. This acquisition, which is comparable to the acquisition of Ernst Hardware in 1960, begins a new era in your company's progress.

We are pleased to announce that the Rhodes acquisition was consummated for only 11,429 shares of Pay'n Save stock, which is considerably less than we had at first estimated. Included in the assets acquired was a life insurance policy with a cash value of over \$250,000 which has now been converted to cash. In addition, Rhodes has substantial loss carry forwards which may be used to reduce taxable income of Rhodes in future years. Most Rhodes employees are being retained and the same standards of salaries and fringe benefits are being extended to these

most welcome new members of the Pay'n Save Family.

Many changes are planned in the Rhodes image, but space does not permit detailing them here. We invite you to "Keep Your Eye on Rhodes," and follow its transformation. Because of the seasonal nature of the department store business and because of the time required to reverse the loss trend, we expect some losses from the operations of the Rhodes stores for the first three quarters of the current year. We anticipate that these losses will be made up in the fourth quarter.

Expansion

The Pay'n Save Drug store opened in March, in Anchorage, has exceeded our expectations. New drug stores were also opened in the University Village of Seattle and on Pacific Highway in Tacoma, Washington. An Ernst Hardware complex was opened in Longview, Washington. The Ernst store in the Aurora Village of Seattle was relocated and enlarged. We are pleased with the Canadian stores in Calgary, Winnipeg and Regina, which are developing very satisfactorily and profits have increased substantially.

Expansion for 1968 includes Pay'n Save stores in Lynnwood, Washington and the Southcenter Shopping Center of Seattle. A number of stores are being remodeled and expanded.

We are now in the process of a major

Major lines of cosmetics and costume jewelry are attractively displayed in distinctive, carpeted, cosmetic departments in each of the Pay'n Save Drug stores.

remodeling and enlargement of the Regina, Canada, Pay'n Save store.

You are invited to visit the new stores, and share our pride in their appearance and we invite your attention to the color photographs on the pages that follow.

Stock Split

The Directors at their meeting held on February 28, 1968 announced that they would recommend a three for one stock split to the stockholders at the annual meeting. The Board at this time also disclosed plans to issue additional common stock to raise approximately \$5,000,000 for future expansion and operating capital. The Board has indicated its intention to declare cash dividends in place of the stock dividends which have been paid for the past five years. No dividends were declared at the February 28th meeting.

Your management is deeply grateful for the sincere loyalty and support of our shareholders, suppliers, customers and our seventeen hundred enthusiastic employees.

Sincerely,

W. L. Dean
Chairman
of the Board

W. L. Dean
President





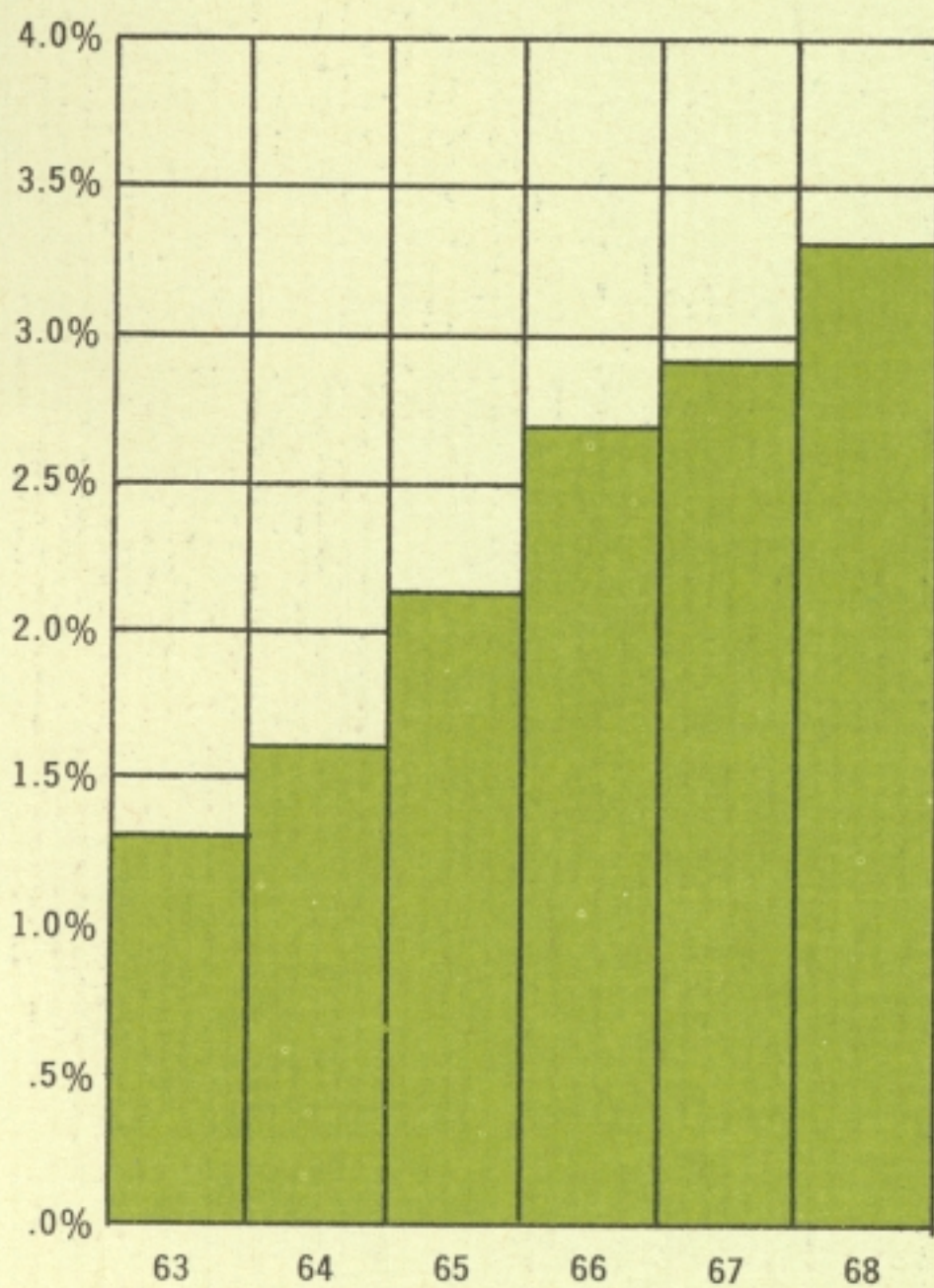
Right; Magnavox Home Entertainment Centers for T.V., radio and stereos are a new feature of the latest Ernst Hardware stores.

Left; Malmo Nurseries provide northwest home owners with quality plants and shrubs in convenient, attractive, self-service displays.

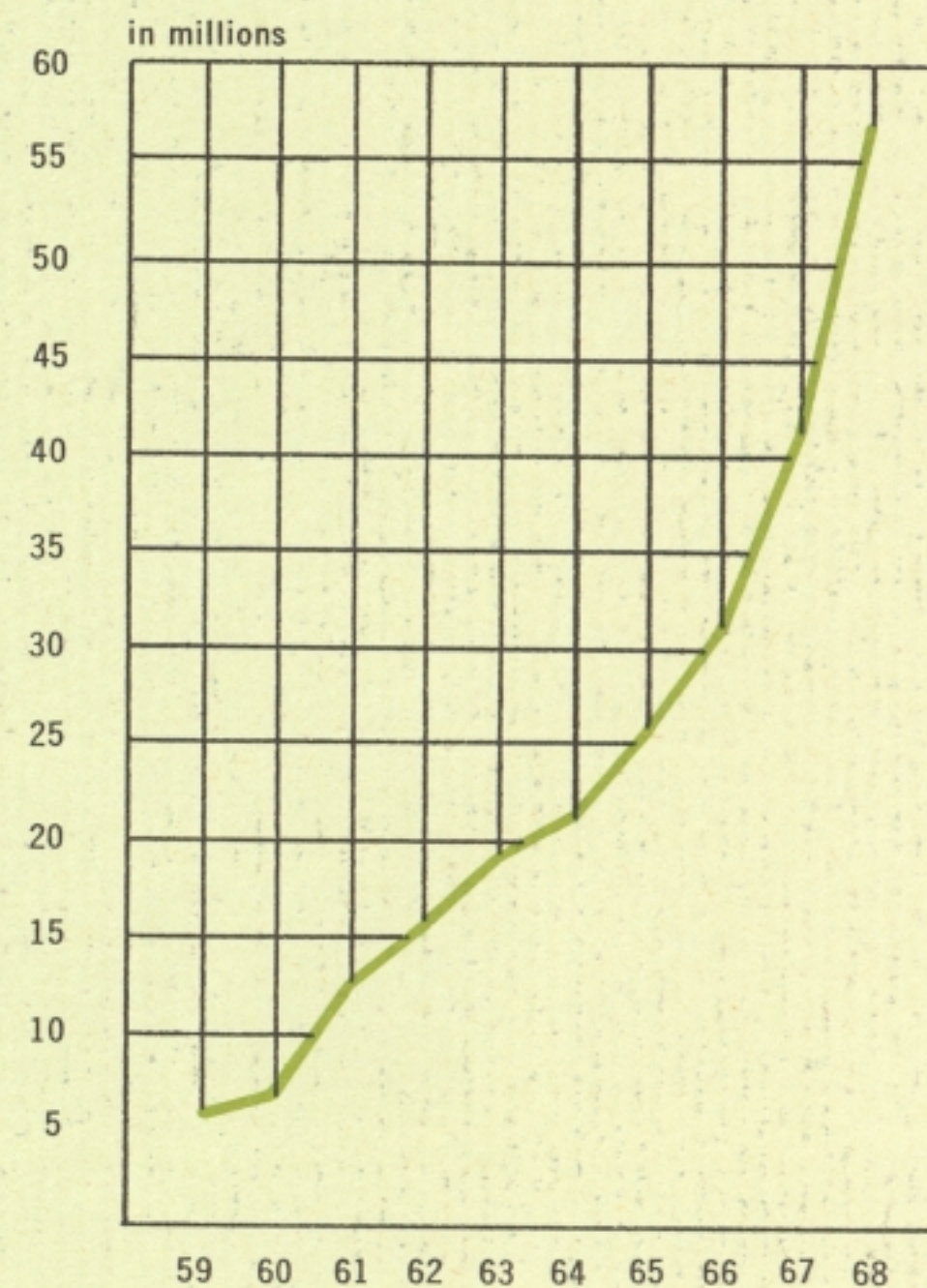
Below; Our sporting goods departments in most Ernst Hardware stores provide the northwest sportsman with quality merchandise for both indoor and outdoor recreation. Many customers are women buying gifts or making selections for their own enjoyment.



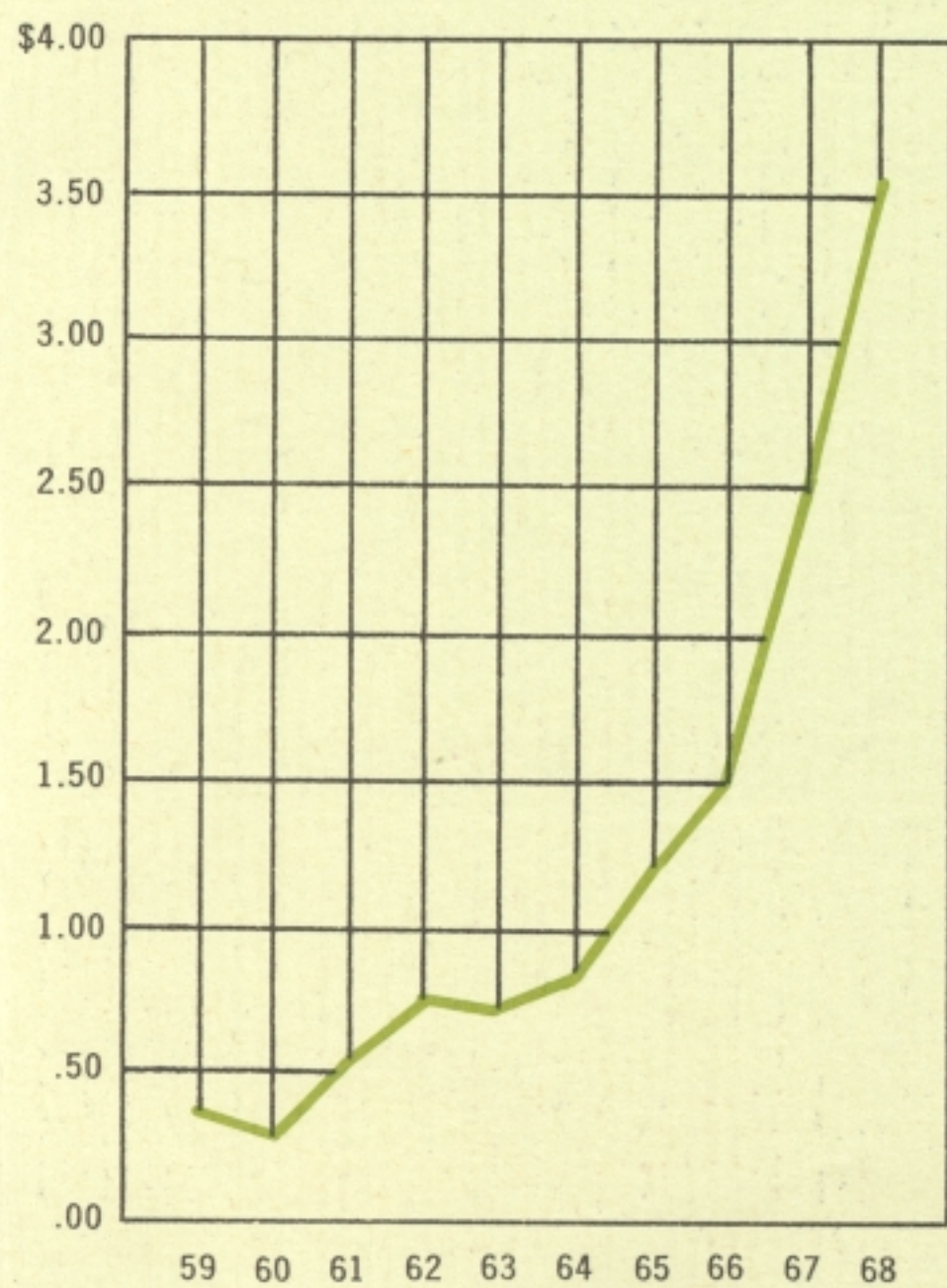
Net Income As a Percentage of Sales



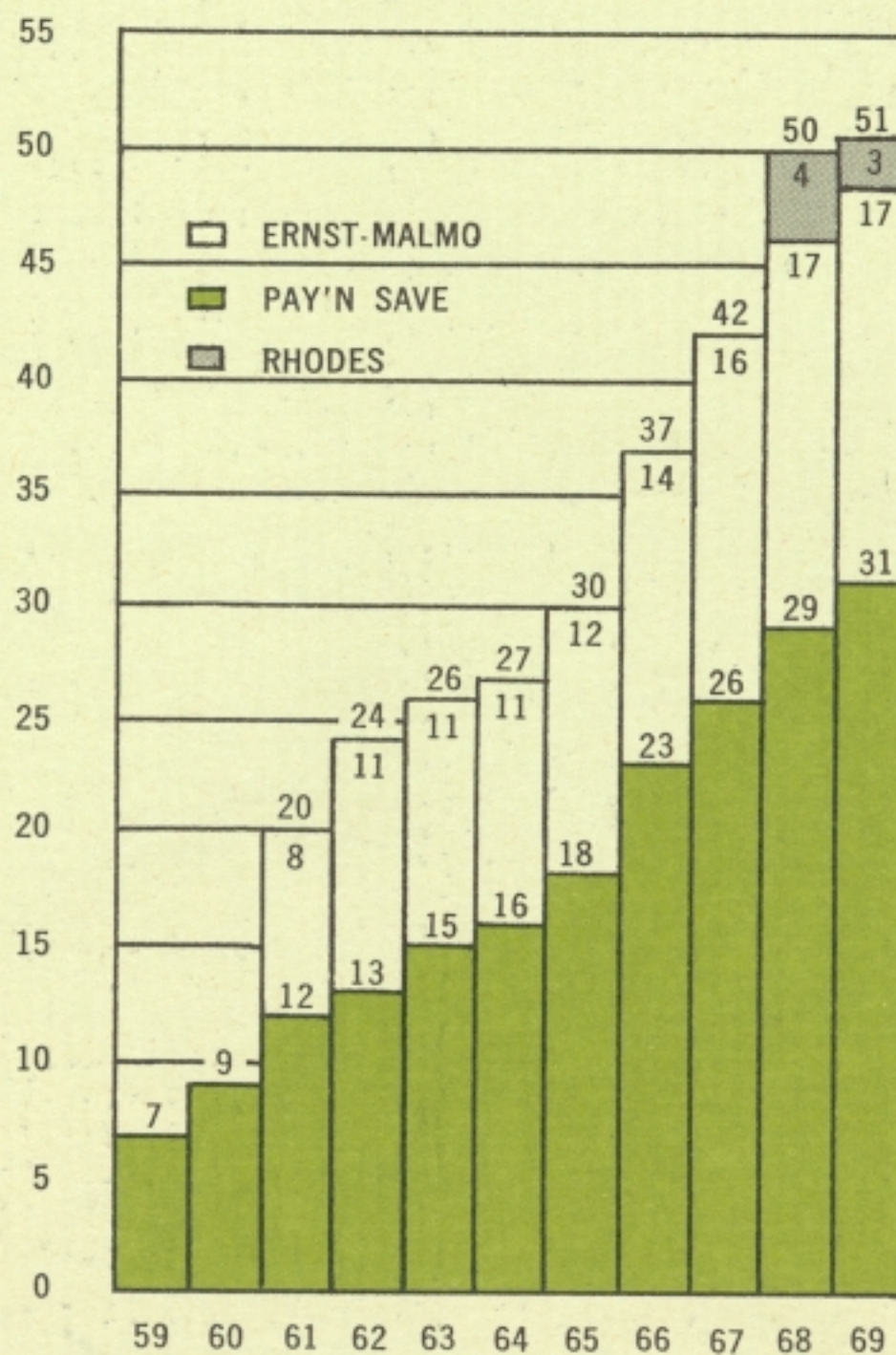
Net Sales



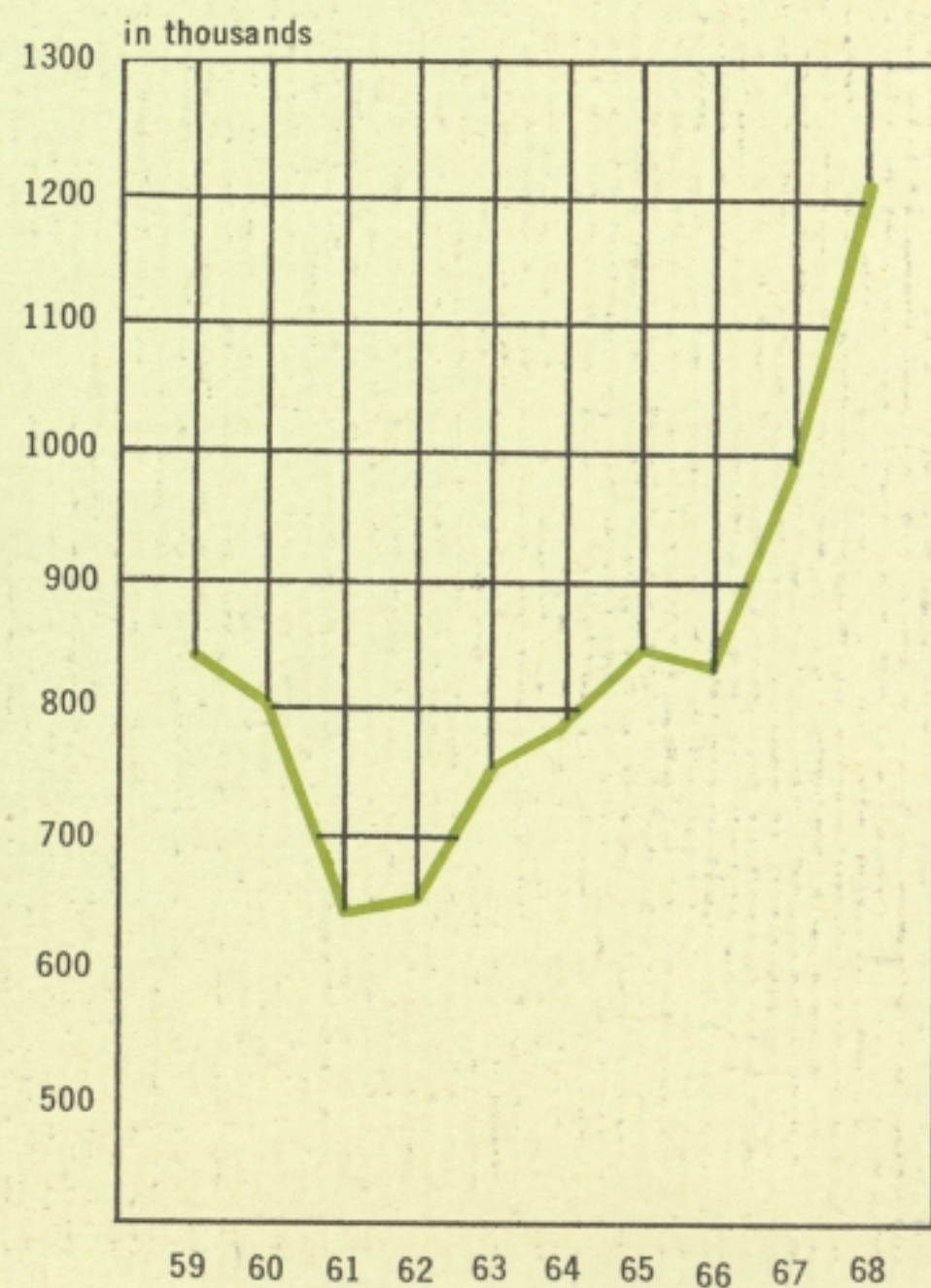
Net Income Per Shares Outstanding



Number of Stores in Operation



Average Sales Per Store



ten year summary of operations

Year ended January 31

	1968	1967	1966	1965	1964	1963	1962	1961	1960	1959
OPERATING RESULTS										
Net Sales*	\$57,574	\$41,672	\$30,943	\$25,247	\$21,375	\$19,956	\$15,779	\$12,879	\$ 7,262	\$ 5,940
Net income*	1,900	1,230	816‡	537	355	263	304	204	131	133
Net Income as a percentage of Sales	3.30%	2.95%	2.64%	2.13%	1.66%	1.32%	1.93%	1.58%	1.80%	2.24%
Earnings on equity	20.8 %	19.8 %	17.6 %	17.7 %	13.7 %	11.8 %	16.9 %	13.9 %	10.2 %	12.5 %
COMMON STOCK										
Net Income per share on average shares outstanding all prior years adjusted for stock dividends	\$ 3.53	\$ 2.45	\$ 1.76‡	\$ 1.25	\$.83	\$.62	\$.78	\$.55	\$.35	\$.39
Book Value per share	16.04	12.69	10.41	8.36	7.26	6.58	5.87	4.86	4.41	3.67
Approximate price range of common stock	61-25	27-15	21-15	15-7½	10-8	12-7	—	—	—	—
Shares outstanding (end of year) †	571	489	449	375	356	339	306	302	291	290
Stock Dividends	5%	5%	5%	5%	5%	—	—	—	—	—
FINANCIAL POSITION (End of Year)										
Working Capital*	\$ 9,275	\$ 7,206	\$ 4,897	\$ 4,132	\$ 3,684	\$ 3,347	\$ 1,809	\$ 1,708	\$ 910	\$ 808
Current Ratio	2.38	2.78	2.33	2.49	2.79	2.53	1.84	2.06	2.58	2.69
Long-Term Debt*	2,652	2,702	1,584	2,239	2,399	2,446	995	72	88	—
Stockholders Equity*	9,153	6,208	4,643	3,133	2,584	2,229	1,797	1,466	1,284	1,065
CAPITALIZATION										
Percentage of Long-term Debt	22.46	30.3	25.4	41.7	48.1	52.3	35.6	4.7	6.4	—
Percentage of Stockholder Equity	77.52	69.7	74.6	58.3	51.9	47.7	64.4	95.3	93.6	100.0
STORES IN OPERATION										
Pay'n Save Drug	26	23	20	18	16	15	13	12	9	7
Pay'n Save Drug Ltd.	3	3	3	—	—	—	—	—	—	—
Ernst Hardware—Malmo Nursery	17	16	14	12	11	11	11	8	—	—
Rhodes Department	4	—	—	—	—	—	—	—	—	—
Total Number of Stores	<u>50</u>	<u>42</u>	<u>37</u>	<u>30</u>	<u>27</u>	<u>26</u>	<u>24</u>	<u>20</u>	<u>9</u>	<u>7</u>
AVERAGE SALES PER STORE (Based upon number of stores at end of the year, excluding Rhodes)*										
	\$ 1,204	\$ 992	\$ 836	\$ 842	\$ 792	\$ 768	\$ 657	\$ 644	\$ 807	\$ 849

* Amount in thousand of dollars.

† Thousands of shares outstanding, adjusted to give effect to stock splits in 1960 and 1962.

‡ Includes non-recurring income of \$87,191 or \$.19 per share in 1966.

Pay'n Save corporation and subsidiary companies

Consolidated Balance Sheet

Assets			Liabilities		
	1968	January 31 1967		1968	January 31 1967
CURRENT ASSETS:			CURRENT LIABILITIES		
Cash	\$ 774,783	\$ 1,124,283	Notes payable—bank	\$ 1,400,000	\$ —
Bank certificates of deposit	137,250	138,750	Accounts payable—trade	3,050,170	2,133,794
Accounts receivable, less allowance for doubtful accounts of \$107,899 and \$36,155, respectively	2,543,869	1,217,530	Withheld and accrued taxes	632,420	413,270
Inventories, at lower of cost or market	12,396,241	8,618,940	Accrued salaries and bonuses	495,657	334,116
Prepaid insurance and miscellaneous	133,468	160,528	Other accrued expenses	296,341	186,621
Total current assets	15,985,611	11,260,031	Current installments on long-term indebtedness	236,107	197,400
INVESTMENTS, at cost:			Federal income taxes	599,529	788,612
Cash value of life Insurance	38,999	25,459	Total current liabilities	6,710,224	4,053,813
Other investments	34,160	22,225	LONG-TERM INDEBTEDNESS—Note 2		
	73,159	47,684	Notes payable	2,770,338	2,310,000
PROPERTY AND EQUIPMENT, at cost—Note 5			Debentures payable	117,438	588,838
Furniture, fixtures and equipment	3,519,299	2,588,893		2,887,776	2,898,838
Leasehold improvements	820,907	556,763	Less—Installments due within one year classified as current liabilities	236,107	197,400
	4,340,206	3,145,656		2,651,669	2,701,438
Less—Accumulated depreciation and amortization	2,137,525	1,763,096	DEFERRED CREDIT—Note 3	45,800	
	2,202,681	1,382,560	STOCKHOLDERS' EQUITY—Notes 2 and 6		
Land	129,400	74,615	Capital stock—authorized 800,000 shares of \$2.50 par value; outstanding 570,748 and 489,013 shares, respectively	1,426,870	1,222,533
	2,332,081	1,457,175	Capital in excess of par value	3,378,644	1,826,766
DEFERRED CHARGES AND OTHER ASSETS	169,684	198,037	Retained earnings	4,347,328	3,158,377
				9,152,842	6,207,676
	\$18,560,535	\$12,962,927	COMMITMENTS—Note 5	\$18,560,535	\$12,962,927

The accompanying notes are an integral part of these financial statements

Pay'n Save corporation and subsidiary companies

statement of consolidated income and retained earnings

	<i>Year ended January 31,</i>	
	<u>1968</u>	<u>1967</u>
Sales and other revenues:		
Net sales	\$57,573,851	\$41,671,839
Interest and other income	220,392	128,697
	<u>57,794,243</u>	<u>41,800,536</u>
Costs and expenses:		
Cost of merchandise sold	40,242,446	29,351,855
Operating and administrative expenses	13,779,009	9,966,021
Interest	205,447	162,537
	<u>54,226,902</u>	<u>39,480,413</u>
Income before federal income taxes	<u>3,567,341</u>	<u>2,320,123</u>
Provision for federal income taxes—Note 3	<u>1,667,000</u>	<u>1,090,000</u>
Net income for the year	<u>1,900,341</u>	<u>1,230,123</u>
Retained earnings at beginning of year:		
As previously reported	3,158,377	2,302,036
Adjustment of prior years' federal income taxes		154,000
As restated	<u>3,158,377</u>	<u>2,456,036</u>
	<u>5,058,718</u>	<u>3,686,159</u>
Stock dividend—5%	<u>(711,390)</u>	<u>(527,782)</u>
Retained earnings at end of year—Note 2	<u>\$ 4,347,328</u>	<u>\$ 3,158,377</u>
Net income per share of common stock—Note 4	<u>\$3.53</u>	<u>\$2.45</u>

The accompanying notes are an integral part of these financial statements

auditors' report

*To the Stockholders of
Pay'n Save Corporation*

In our opinion, the accompanying consolidated balance sheet and related statement of consolidated income and retained earnings present fairly the financial position of Pay'n Save Corporation and its' subsidiaries at January 31, 1968 and the results of their operations for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year. Our examination of these statements was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

PRICE WATERHOUSE & Co.

Seattle, Washington
March 2, 1968

Pay'n Save corporation and subsidiary companies

notes to financial statements January 31, 1968

NOTE 1 — BASIS OF CONSOLIDATION

The financial statements include the accounts of Pay'n Save Corporation and its subsidiaries, all of which are wholly-owned. One of the subsidiaries, Rhodes Department Stores, was purchased November 1, 1967 and only the results of its' operations since acquisition are included in the statement of income and retained earnings.

NOTE 2 — LONG-TERM INDEBTEDNESS

Long-term indebtedness comprised the following:

	<i>January 31</i>	
	<i>1968</i>	<i>1967</i>
Notes payable to:		
Insurance companies	\$2,250,000	\$2,275,000
Others	520,338	35,000
	<u>\$2,770,338</u>	<u>\$2,310,000</u>
6% subordinated debentures	\$ 49,438	\$ 124,838
5½% convertible subordinated debentures	68,000	464,000
	<u>\$ 117,438</u>	<u>\$ 588,838</u>

The notes and debentures are unsecured, except for a real estate contract in the amount of \$102,000. The various financing agreements place certain restrictions upon the creation of additional debt, require the maintenance of at least \$4,000,000 of working capital and limit the payment of cash dividends and the purchase or redemption of capital stock to an amount equal to the excess of retained earnings over \$2,002,036. Deferred financing costs are being amortized over the lives of the respective debt substantially on the basis of the obligations outstanding.

The notes payable to insurance companies are due in annual installments on August 1 each year to 1981 and range from \$50,000 to \$225,000. The note agreements permit advance payments without premium under certain circumstances.

The 6% subordinated debentures are payable on December 31, 1968. The 5½% convertible debentures may be converted into common stock at \$12.25 per share to July 31, 1968; if not converted, they will be redeemed at that date.

A summary of maturities of long-term indebtedness for the five years ending January 31, 1973 follows:

<i>Year ending January 31</i>	<i>Notes— Insurance Companies</i>	<i>Notes— Others</i>	<i>Debentures</i>	<i>Together</i>
1969	\$ 50,000	\$ 68,669	\$117,438	\$ 236,107
1970	125,000	72,394		197,394
1971	125,000	76,261		201,261
1972	125,000	80,357		205,357
1973	175,000	77,694		252,694
	<u>\$600,000</u>	<u>\$375,375</u>	<u>\$117,438</u>	<u>\$1,092,813</u>

NOTE 3 — INCOME TAXES

Wholly owned subsidiaries, Rhodes Department Stores and Pay'n Save Drugs Ltd., have substantial loss carry forwards which may be used to reduce taxable income of the subsidiaries in future years. The Accounting Principles Board of the American Institute of C.P.A.'s adopted procedures in 1967 which revised the accounting for income taxes and require that any tax reduction, resulting from losses prior to acquisition of subsidiaries, be reflected in the accounting for the initial acquisition. In compliance with these procedures, the company plans to provide for income taxes (which will not be payable) in its statement of income and a deferred credit in the amount of any tax saving resulting from the loss carry forwards. The deferred credit will be amortized over five years. Accordingly, provision of \$52,000 has been made in the statement of income for income taxes which will not be payable and \$6,200 has been amortized to income.

At January 31, there were remaining preacquisition loss carry forwards of approximately \$1,450,000.

NOTE 4 — EMPLOYEE STOCK OPTION PLANS

The company has a stock option plan, established in 1962, under which options had previously been granted for all stock reserved under the plan. Option prices are based on the fair market value of the stock at the time the options were granted, adjusted for the effect of stock dividends. Options were exercised for 12,436 shares during the year at prices ranging from \$8.00 to \$9.48. Options for 18,564 shares, at prices ranging from \$6.25 to \$21.45, remained outstanding at January 31, 1968.

During the year, the company adopted a new plan under which 35,000 shares of the company's common stock is reserved. Option prices may not be less than the market value of the shares at the time of granting of the option and options may not be granted for more than 2,500 shares to one person. Options may not be exercised for two years and must be exercised within five years. During the year, options for 6,100 shares were granted at the option price of \$25.375, of which options for 350 shares were cancelled due to resignations.

Additionally, options for 1,000 shares at \$25.375 were granted to both the Chairman of the Board and the President, who do not participate in the plan adopted during the year.

Based upon the assumption that all stock options and convertible debentures outstanding at January 31, 1968 had been exercised or converted at the beginning of the year and the proceeds invested at normal interest rates, the net income per share would have been \$3.36.

NOTE 5 — PROPERTY AND EQUIPMENT

The company's operations are conducted on leased premises. Leases are generally for periods of from ten to twenty years and, in most cases, provide for minimum rentals plus additional amounts based on a percentage of sales. The company also leases certain store furniture and equipment; such leases are for periods of ten years. Minimum annual rentals under the terms of leases in effect at January 31, 1968 are approximately \$1,875,000.

Provision is made for depreciation of furniture, fixtures, and equipment by the double declining method, except as to subsidiaries which use the straight line method, over the expected life of the assets. Leasehold improvements are amortized over the period of the leases. The total provision for depreciation and amortization for the current year amounted to \$364,622 as compared with \$258,241 in the prior year.

NOTE 6 — CAPITAL STOCK AND CAPITAL IN EXCESS OF PAR VALUE

Transactions in capital stock and capital in excess of par value during the year ended January 31, 1968 are summarized below:

	Capital Stock		Capital in Excess of Par Value
	Shares	Amount	
Balance, January 31, 1967	489,013	\$1,222,533	\$1,826,766
April, 1967 stock dividend—5%, at fair market value	24,744	61,860	649,530
Conversion of \$361,000 of debentures, at conversion prices net of initial debenture issue costs	33,126	82,815	248,381
Exercise of employee stock option	12,436	31,090	82,539
Purchase of Rhodes Department Stores, at fair market value of shares	11,429	28,572	571,428
Balance, January 31, 1968	<u>570,748</u>	<u>\$1,426,870</u>	<u>\$3,378,644</u>

Right; Green lawn, and beautiful fountains accent the main entrance to the Rhodes Department store in the Crossroads Shopping Center of Bellevue, Washington.



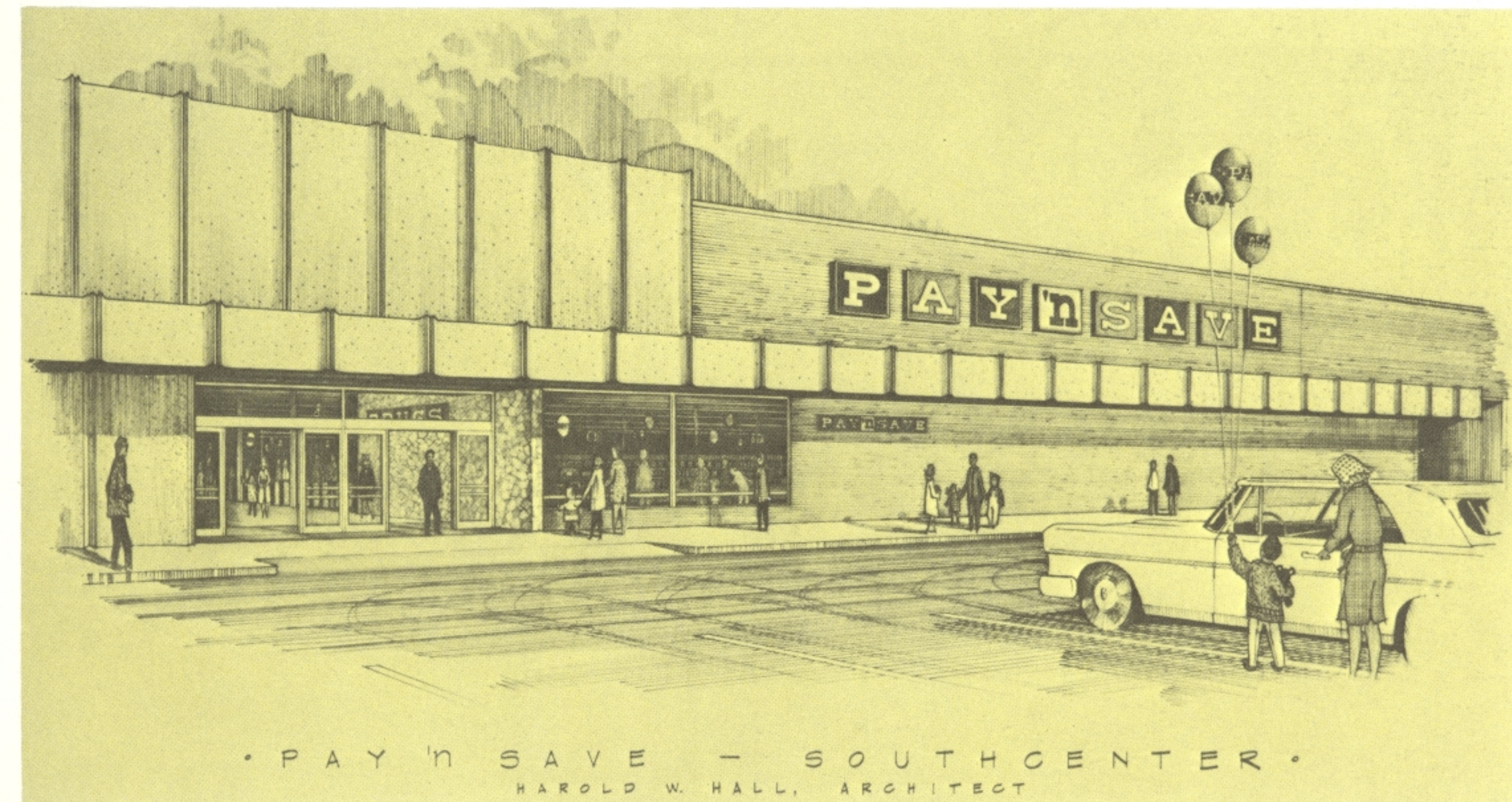
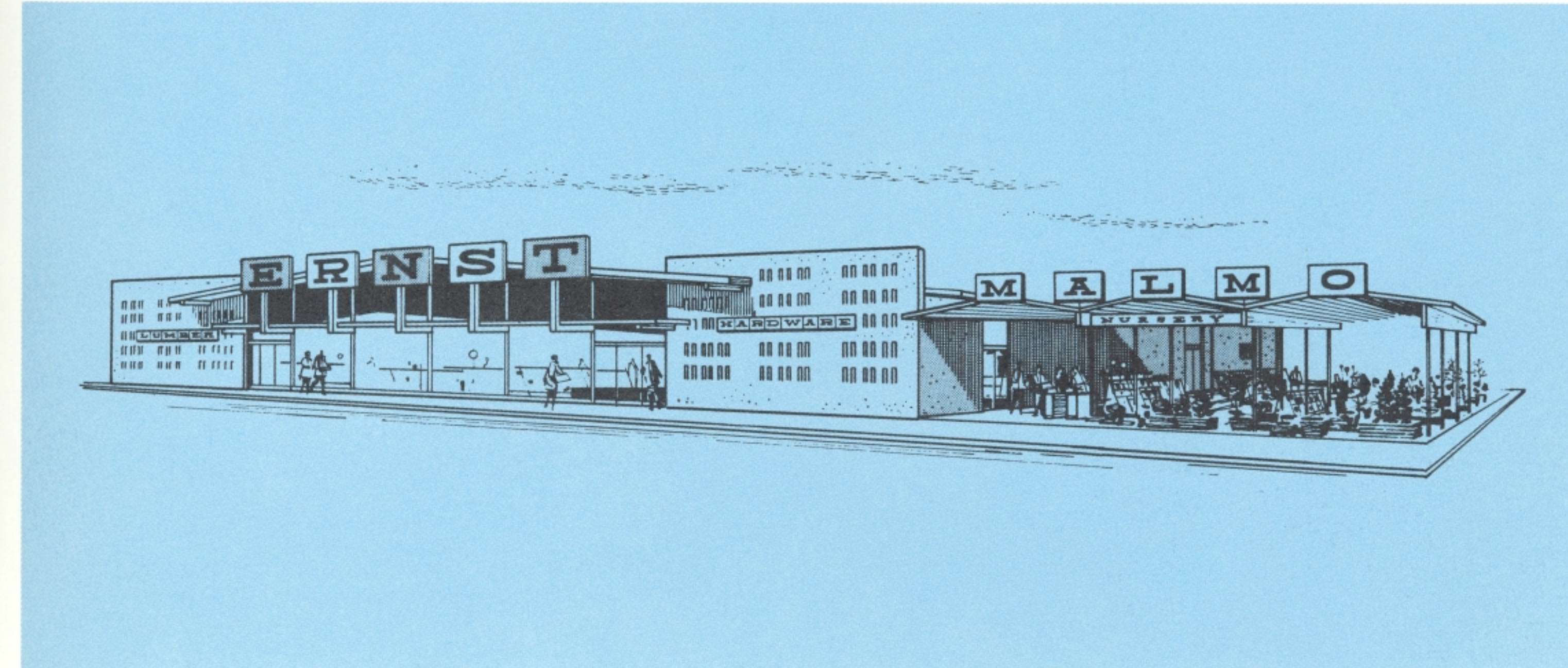
Below; The dispensing of prescriptions continues to be of increasing importance to the Pay'n Save Drug stores. Wide aisles and clean, uncluttered, low profile display counters; convenience features in all of the drug stores, are illustrated.





Left; Displays of Greeting Cards for all ages and all occasions, build profitable traffic for the entire store.

Below; Well trained, pleasant cashiers, invite customers to make their selections from carefully chosen impulse items.



locations

ERNST HARDWARE STORES:

1	6th and Pike Street	Seattle
2	4314 W. Alaska (West Seattle)*	Seattle
3	4704 25th N.E. (University Village)*†	Seattle
4	414 Northgate Mall*†	Seattle
5	1740 Market Street (Ballard)	Seattle
6	815 First Avenue	Seattle
7	125 106th N.E.*†	Bellevue
8	20050 Aurora Village Square N.	Seattle
9	333 Westlake Ave. N.	Seattle
10	4920 Evergreen Way*†	Everett
11	10419 Plaza Dr. S.W. (Lakewood)*†	Tacoma
12	9109 Westwood Village S.W.*†	Seattle
13	60 Grady Way (Renton Village)*†	Renton
14	25 South Sound Center*†	Olympia
15	150 Burien Plaza (Burien)*†	Seattle
16	Triangle Shopping Center*†	Longview

MALMO NURSERY STORES:

1	150th and Aurora Avenue North	Seattle
---	-------------------------------	---------

MALMO WHOLESALE NURSERY:

1	14900 Stone Avenue	Seattle
---	--------------------	---------

RHODES DEPARTMENT STORES:

1	Second and Union (Downtown)	Seattle
2	2700 N.E. Village Mall (University Village)	Seattle
3	17171 Bothell Way N.E. (Forest Park)	Seattle
4	N.E. 156th and 8th N.E. (Crossroads)	Bellevue

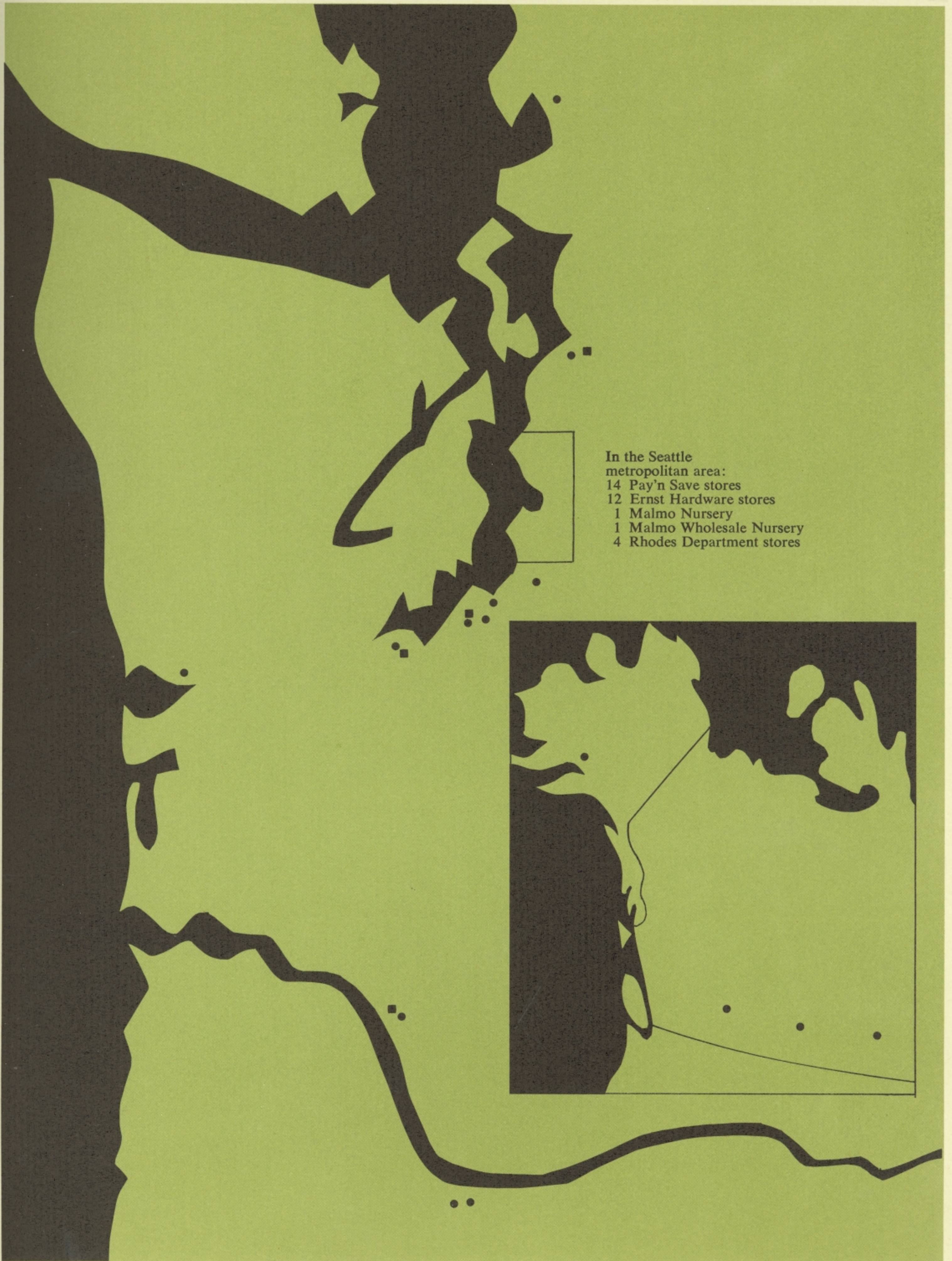
*Store includes Malmo Nursery department
†Store includes Pre-Cut Lumber department

PAY'N SAVE DRUG STORES:

No.	Store Address	
1	319 Pike Street	Seattle
2	2711 Colby Avenue	Everett
3	4535 University Way N.E.	Seattle
4	412 Northgate Mall	Seattle
5	1423 Market Street (Ballard)	Seattle
6	1400 Cornwall	Bellingham
7	250 S.W. 152nd Street (Burien)	Seattle
8	201 S. Broadway	Aberdeen
9	8500 35th N.E. (Wedgewood)	Seattle
10	20220 Aurora Ave. (Aurora Village)	Seattle
11	1421 Lloyd Center	Portland
12	4100 S.E. 82nd Ave. (Eastport Plaza)	Portland
13	Triangle Shopping Center	Longview
14	7707 S.E. 27th	Mercer Island
15	120 106th Ave. N.E.	Bellevue
16	2707 Rainier Ave. S.	Seattle
17	202 Cross St. S.E.	Auburn
18	17171 Bothell Way N.E. (Forest Park)*	Seattle
19	40 Grady Way (Renton Village)	Renton
20	9071 Westwood Village S.W.	Seattle
21	6111 Sixth Avenue	Tacoma
22	415 South Sound Center	Olympia
23	10407 Plaza Dr. S.W. (Lakewood)	Tacoma
24	1370 Northern Lights Boulevard	Anchorage
25	4700 University Village Pl.	Seattle
26	9830 Pacific Ave. S.	Tacoma

PAY'N SAVE DRUGS LTD.:

1	326 7th Avenue West	Calgary, Alberta
2	318 Donald Street	Winnipeg, Manitoba
3	1926 Hamilton Street	Regina, Saskatchewan



In the Seattle
metropolitan area:
14 Pay'n Save stores
12 Ernst Hardware stores
1 Malmo Nursery
1 Malmo Wholesale Nursery
4 Rhodes Department stores

**transfer agent
and registrar**

Peoples National Bank of Washington

counsel

Ryan, Carlson, Bush, Swanson, and Hendel

auditors

Price Waterhouse & Co.

general offices

1511 6th Avenue
Seattle, Washington 98101

PAY'n SAVE

PAY'N SAVE DRUG STORES
ERNST HARDWARE STORES
MALMO NURSERY STORES
RHODES DEPARTMENT STORES
PAY'N SAVE DRUGS, LTD.