

Palmer G. Lewis Co., Inc.
Annual Report
Nineteen Eighty-Four

ANNUAL REPORTS
Palmer G. Lewis Co., Inc. 1984

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"A Leading
Distributor
of Building
Related
Products in
the West"

Lewis (Palmer G.) Co., INC.

1984

Palmer G. Lewis

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The Company's Common Stock is traded on the Over-The-Counter market under the NASDAQ symbol LWIS. The following table shows the cash dividends paid or declared and the high and low selling prices for the PGL Common Stock for each fiscal quarter of 1985 and 1984 as reported for National Market Issues. (Prior to November 22, 1983, the prices reported are the high and low bid prices.) Prices and dividends per share have been adjusted for 4% stock dividends in September, 1984 and September, 1983 and rounded to the nearest $\frac{1}{8}$.

*Quarterly
Stock Prices*

Fiscal Period	Selling Price		Dividends Per Share
	High	Low	
1984 1st Quarter	\$ 13	\$ 10 $\frac{1}{8}$	\$.06
2nd Quarter	13 $\frac{3}{8}$	9 $\frac{3}{4}$.07
3rd Quarter	10 $\frac{3}{8}$	8 $\frac{3}{4}$.07
4th Quarter	10 $\frac{1}{2}$	8 $\frac{3}{8}$.07
1985 1st Quarter	10	7 $\frac{1}{2}$.07
2nd Quarter	7 $\frac{7}{8}$	7 $\frac{1}{8}$.07
3rd Quarter	9 $\frac{1}{8}$	7 $\frac{1}{8}$.07
4th Quarter	9 $\frac{1}{2}$	7 $\frac{1}{8}$.07

The Company

Palmer G. Lewis Co., Inc. is a wholesale distributor of building related materials. With its four PGL divisions, it distributes a broad line of basic building materials through 14 service centers from central California to Alaska. Sea-Pac Sales Company, a recently acquired

subsidiary with five locations, distributes Armstrong floor coverings, Gibson appliances and Sharp Microwave ovens, TV's and VCR's throughout the Northwest. PGL's subsidiary, Cochrane Northwest Inc., operates three locations in Washington serving the

high pressure laminate and floor covering accessory market. The Company also operates Truck Service Inc., a truck repair shop in Kent, Washington.

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Financial Highlights

Years Ended	Jan. 25, 1985	Jan. 27, 1984	% Change
Net Sales	\$144,382,029	\$121,043,541	+19
Net Income	\$ 1,072,831	\$ 1,820,177	-41
Net Income Per Share	\$.31	\$.67	-54
Cash Dividends	\$.28	\$.27	+ 4
Stock Dividends	4%	4%	—
Total Assets	\$ 53,403,183	\$ 42,489,908	+26
Stockholders' Equity	\$ 33,178,934	\$ 27,028,707	+23
Average Shares Outstanding	\$ 3,500,174	\$ 2,719,624	+29

Net income per share and average shares outstanding during the year have been adjusted for the 4% stock dividend paid in September 1984 and September 1983.

Robert D. Peterson

At the conclusion of the reporting year, January 25, 1985, Robert D. Peterson retired as Chief Executive Officer of the Palmer G. Lewis Company.

A native of Minneapolis, Bob received his B.S. Degree in Forestry from the University of Minnesota and his Master's Degree from the University of Washington. After college, he served three years as a Communications Officer in the U.S. Army Air Force.

Bob joined the fledgling Palmer G. Lewis Company in 1946—as its first full time salesman. At that time the Company had one location and annual sales of \$777,000. In 1952, when Bob became Sales Manager, the Company had 2 locations with total sales of \$1.5 million. In 1960 he became Executive Vice President and General Manager, and in 1967 Bob

was appointed President and Chief Executive Officer. By the time he was elected Chairman of the Board in 1979 the Company had grown to 22 locations throughout the West and Alaska, and sales had grown to \$105 million.

Bob's leadership has been evident throughout the building material distribution industry. He and the Company have repeatedly been honored by industry peers as the best building material wholesaler in the business.

Bob has often said of the Company's founder, Palmer Lewis—"A man is extremely fortunate if he is lucky enough to be associated with someone in business who can inspire him and set the type of example that will bring out the best in himself." The employees at PGL have enjoyed that same kind of



inspirational leadership from Bob during the 39 years that he has served the Company.

The shareholders and the Company are fortunate that Bob has agreed to continue to serve as Chairman of the Board of Directors.

*John N. Anderson
Vice Chairman
Chief Executive Officer*

*Message to
PGL Shareholders*

Last year was a mixed bag of successes, disappointments and changes at PGL. Although sales, due to an acquisition, hit a new record of \$144 million, they fell short of the goals which had been set. Profits also fell, and earnings per share were affected even more because additional shares had been issued.

Let's review the operations as they occurred in 1984. It was decided to close the Eugene, Oregon and Redding, California warehouses. Considering ongoing economic problems in the Eugene area, the Company purchased the GH Foster Company in Medford (Southern Oregon) and eliminated the Eugene and Redding branches. These moves enabled PGL to more efficiently serve the Oregon and Northern California markets from Portland, Medford and Sacramento. There were significant costs involved in the closing of the existing warehouses and, frankly, the GH Foster acquisition had a negative effect on 1984 earnings. The Medford branch should see a turnaround in 1985.

The acquisition of Sea-Pac Sales in May has proven to be extremely beneficial to PGL. Sea-Pac,

while in the distribution business, covers a different product and customer base than PGL has historically had. It is a self-sufficient subsidiary which has met its expectations, and was a significant contributor to PGL earnings in 1984.

Cochrane Northwest Inc. had a disappointing year. The Bellevue, Washington branch was closed, and the Tacoma headquarters were moved to Seattle. PGL has completed the purchase of the minority interests in CNI, and it will be operated as a wholly-owned subsidiary in the future. With major expenses recognized in 1984, CNI should prove profitable in 1985. The Alaska Division of PGL had a moderately strong first quarter in 1984, but took a substantial downward turn with the Alaska economy during the balance of the year. Housing has been projected to improve slightly during the 1985 construction season in Alaska.

The major challenge in the PGL operating divisions is the Company's Oregon Division. The forest products industry in the Northwest has suffered staggering blows, and the Oregon economy has been slow to recover. This Division is receiving special

management attention in order to make it a satisfactory profit performer.

At the Corporate level a great deal has been accomplished in 1984. The completion of on-line computer services through all branches and subsidiaries was substantially completed. Deflated inventory values, questionable assets and marginal receivables have been recognized as write-downs.

As the Company's new Chief Executive Officer, it is my duty to report what has happened, where we are now, and where we are going. I believe PGL is one of the strongest companies in our industry, both as to financial condition and earnings potential. The Company's net worth is the highest it has ever been. In spite of poor earnings during the past four years, the cash flow, after depreciation from Company owned assets, has been growing steadily. In addition, our assets are worth considerably more than the book value shown. Long-term debt is minimal, and our short-term borrowing varies from zero to moderate, depending on the time of the year.

PGL has clearly been very sensitive to interest rates, and that has worked

against it for the past four years. This has been especially noticeable in the past year when short-term rates dropped dramatically but mortgage rates remained high.

The building material distribution business is a business that is here to stay, because it provides an essential function for both the manufacturer and the retail dealer. The business has changed dramatically, and it will continue to change, but the function is still essential. Our challenge is to review our distribution methods, the products which are distributed and the customers served, so that we can operate profitably at what are becoming "normal" higher rates of interest. If rates drop, and sales therefore increase, so much the better. In the meantime, we will be striving for the balance which will produce satisfactory profits at any existing level of interest rates. Every asset in the Company will be evaluated for its contribution to profit, both in the short and long term.

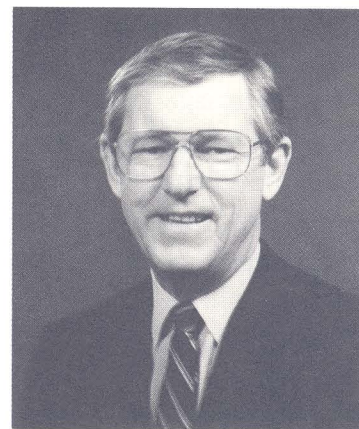
The goal of PGL is to produce an excellent return to the shareholders. Any public company must do that to justify the shareholders' investment. Although PGL

has not achieved this goal in recent years, it has historically been an excellent investment for medium to long term investors. I believe PGL will continue to justify investor confidence in the future. To repeat—our goal in the immediate future is NOT an increase in size through acquisition, but rather an improvement in profit performance within our existing businesses. After that has happened, we will again be looking toward growth outside of our present business shell.

The challenge we face will not be solved overnight. Some important changes have occurred in 1984, and many more refinements and changes will be achieved in 1985 and beyond. In an industry which surely has never been described as glamorous, we are finding a high degree of excitement in meeting this challenge for performance excellence. We have the people, the company and the determination to make it happen.



John N. Anderson
Vice Chairman
Chief Executive Officer



John N. Anderson
Vice Chairman and
Chief Executive Officer



Richard E. Lundgren
President and Chief
Operating Officer

*Management's
Discussion
and Analysis*

Operations

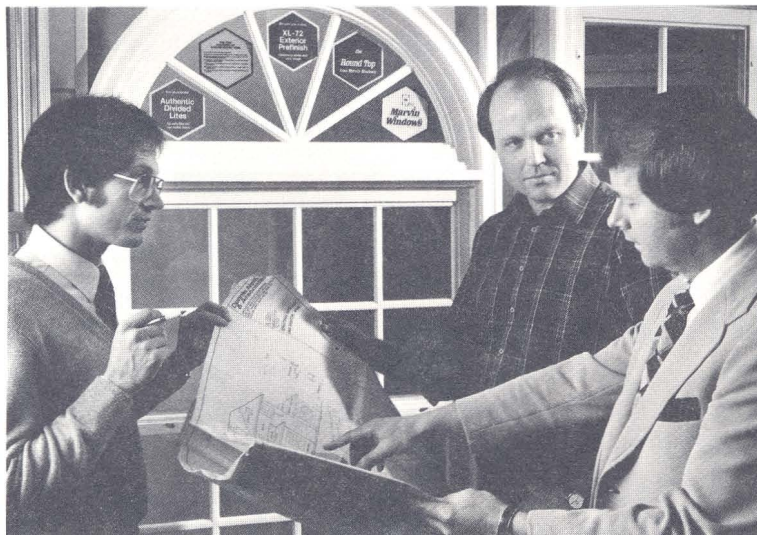
Sales for fiscal year 1985 totaled \$144.4 million, up 19% when compared to the \$121.0 million for fiscal 1984. The sales results in fiscal 1984 were up 17% from the \$103.5 million for fiscal 1983. In the three years prior to fiscal 1984, the Company's sales and earnings were adversely affected by a recession in the building industry. In fiscal 1985, inflation was not a factor in most of the Company's product lines. The Company experienced deflation in many of its commodity lines.

The acquisition of Sea-Pac Sales in May, 1984 was responsible for the entire increase in the Company's sales volume. Without the \$24.7 million contributed

by Sea-Pac, sales results would actually have been down by 1%. The first quarter of fiscal 1985 started out strong. However, rising interest rates beginning in May, 1984 curtailed sales growth. As a result of falling demand for building material products, intense competition had a negative effect on gross profit margins. In the case of many commodity items, the Company actually experienced inventory losses as a result of falling prices.

The Company experienced softening of business throughout its marketing area. The Alaska economy, which had been strong through the previous four fiscal years, had an extreme downturn, and sales results for the last three quarters

Marvin Windows are fast becoming the choice for quality windows and doors. Here PGL Marvin window sales personnel examine blueprints for Marvin requirements with customer.



of the year were off by approximately 25% from fiscal 1984. The increase in cost and expenses for the Company in the current fiscal year includes the added costs of Sea-Pac Sales. Without Sea-Pac, expenses were up modestly.

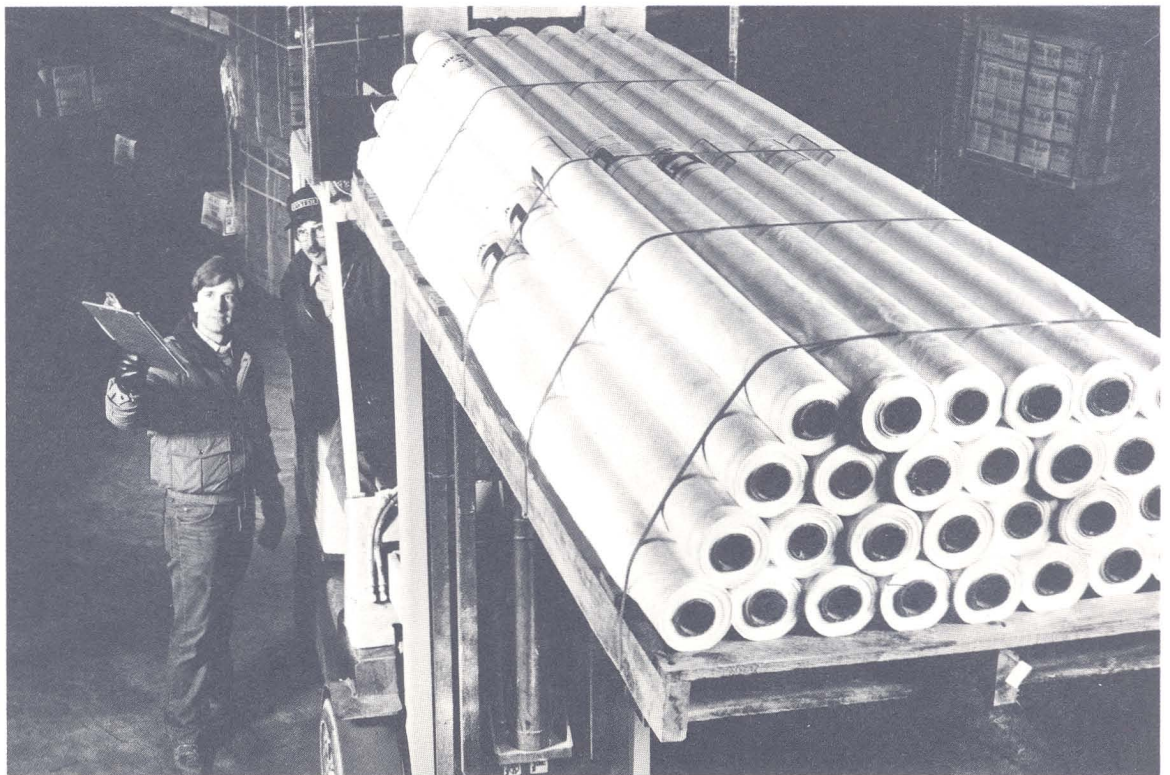
The Company is working hard to curtail costs and has been closing marginal operations over recent years. In the last year it closed three branches. However, during that period the Company also acquired a branch in Medford, Oregon. The costs of closing three branches and integrating a new acquisition into the Company's operations also had a negative impact on operating expenses. Interest costs, which in fiscal

1984 reached a recent low point of under \$1 million, grew to \$1,346,000 in fiscal 1985, a result of higher interest rates and higher borrowing. In the fourth quarter of fiscal 1985 the Company also wrote-down marginal assets on its balance sheet which had a pre-tax effect on income in excess of \$700,000.

As a result of the above, net income, in spite of the positive contribution of Sea-Pac Sales, dropped by 41% in fiscal 1985. Net income for fiscal 1984 of \$1.8 million represented a substantial improvement over the two previous years, which were adversely affected by the recession. Because of lower earnings and higher investment tax credits than experienced in

previous years, the Company's income tax rate in fiscal 1985 was substantially reduced. This lower rate had a positive effect on net income in the current year. Per share results showed a larger decline in the current fiscal year due to the additional 747,732 shares outstanding as a result of the acquisition of Sea-Pac.

Tyvek, developed and manufactured only by DuPont, offers superior performance as an air infiltration barrier for wrapping house exteriors. Tyvek is available in 9' and 3' rolls.



Dividends

The Company continues to pay cash dividends of \$.28 per share (\$.07 per quarter), the same rate as it has paid over the past five fiscal years. Dividend data has been restated downward to reflect the effect of the 4% stock dividend that the Company has paid since 1968. The Company has paid uninterrupted cash dividends every year since it initiated its dividend policy 25 years ago.

Balance Sheet Data

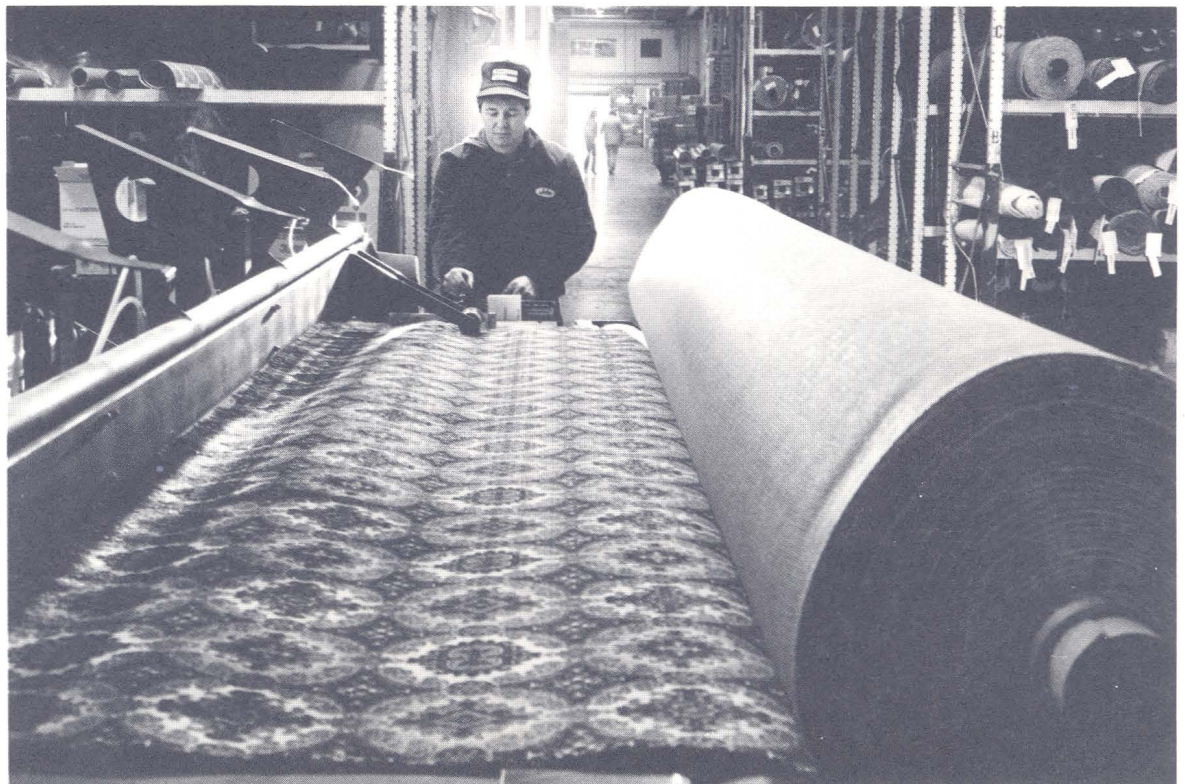
The Company's balance sheet continues to be one of the strongest in its industry. Its stock offering of 880,000 shares in fiscal 1984, which raised approxi-

mately \$9.5 million in cash, was a main contributor to this strength. The acquisition of Sea-Pac Sales, which in its own right had an extremely strong balance sheet, was primarily for stock and as a result did not detract from the Company's financial condition. Even with the cash expended for the Sea-Pac Sales and Medford Branch acquisitions, the Company's working capital increased approximately \$2 million. During the year the Company had lines of credit with banks to borrow up to \$24 million under nonsecured arrangements. The Company's short-term borrowing



Above Right
For over 12 years, Sea-Pac Sales Company has been the sole distributor in the Northwest for Sharp and Gibson home appliances. Sharp quality products include microwave ovens, televisions, and video recorders.

Right
Sea-Pac Sales Company is the exclusive Armstrong carpet distributor for the entire Northwest.



peaked at slightly over \$13 million for the year, up substantially from the \$5.6 million in fiscal 1984, after the stock offering. In previous fiscal years the Company's borrowing peaked in the \$10-\$13 million ranges. Long-term debt for the corporation continues to be modest.

Other Data

During the year the Company was able to rent most of the branches that were idle because of closures. Many of these rental agreements provide the renter an option to acquire the facility at levels which would result in significant gains to the Company if exercised.

The Company's Profit Sharing Plan continues to grow, although contributions for the year declined as a result of the less than satisfactory Company earnings. The Profit Sharing Plan income, including forfeitures, exceeded 14% on its investments. The Company also made a contribution to its Employee Stock Ownership Plan (PAYSOP) as authorized under the Internal Revenue Code. This allows a tax credit for Company stock distributions into trust for its employees. Approximately \$48,000 was set aside in fiscal 1985 for this program.

The Company's employ-

ment at year-end totaled 492 employees. Without the Sea-Pac Sales' employees, the Company's employment dropped by approximately 2%. The majority of employees are enrolled on a continuous basis in the Company's Employee Stock Purchase Plan and a significant majority are shareholders of the Company.

Above Right
Truck Service
Inc., provides
expert truck
repairs and dis-
tributes truck
parts to PGL and
the many other
fleets located in
the area.

Right
Workman at Coch-
rane Northwest,
Inc., operates a tub-
bending machine
which applies heat
and pressure to
shape laminate to
fit the configur-
ation of a bathtub
opening.

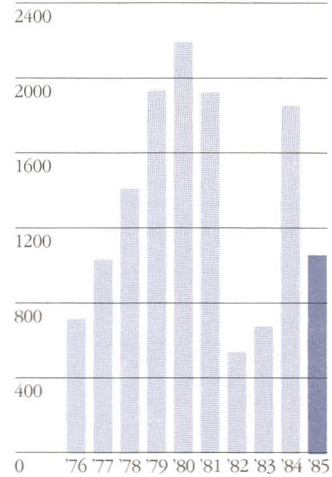


*Selected Consolidated
Financial Information*

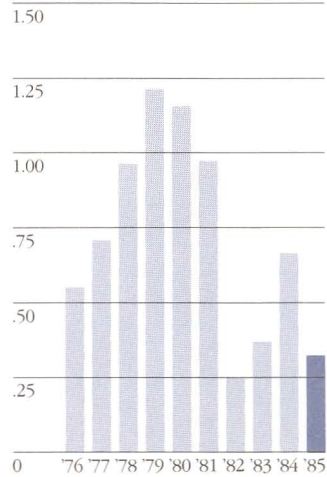
Fiscal Years Ended January	1985	1984	1983	1982	1981
Income Statement Data:					
Net Sales	\$144,382,000	\$121,044,000	\$103,497,000	\$111,192,000	\$95,478,000
Gross Profit %	18.4%	18.9%	19.0%	17.0%	19.1%
Interest Expense	1,346,000	982,000	1,725,000	2,384,000	1,761,000
Depreciation & Amortization	2,080,000	1,599,000	1,397,000	1,291,000	1,174,000
Income Taxes - Continuing Operations	249,000	1,059,000	335,000	329,000	998,000
Net Income:					
Continuing Operations	1,073,000	1,820,000	678,000	488,000	1,289,000
Discontinued Operations	—	—	—	—	(20,000)
Sales of Discontinued Operations	—	—	—	—	616,000
Net Income	1,073,000	1,820,000	678,000	488,000	1,885,000
Net Income Per Share	.31	.67	.34	.25	.97
Average Shares Outstanding	3,500,000	2,720,000	1,981,000	1,972,000	1,947,000
Dividends Per Common Share:					
Cash	.28	.27	.26	.25	.24
Stock	4%	4%	4%	4%	4%
Balance Sheet Data:					
Total Assets	53,403,000	42,490,000	38,966,000	38,213,000	40,187,000
Working Capital	19,816,000	17,501,000	8,115,000	11,226,000	9,676,000
Long-Term Debt (net of Current Portion)	2,526,000	2,236,000	2,360,000	5,341,000	5,634,000
Capitalized Leases (net of Current Portion)	2,413,000	2,525,000	2,620,000	2,706,000	2,767,000
Stockholders' Equity	33,179,000	27,029,000	16,490,000	16,291,000	16,130,000
Other Data:					
Net Capital Expenditures	3,648,000	1,846,000	1,579,000	1,116,000	1,544,000
Cash Flow (net income + non-cash items)	3,149,000	3,418,000	2,049,000	1,773,000	2,476,000
Profit Sharing Trust Value	5,173,000	5,165,000	4,778,000	4,288,000	4,340,000
Profit Sharing Disbursements	820,000	452,000	755,000	313,000	353,000
Number of Employees (continuing operations)	492	403	369	363	391
Net Income:					
As a % of Average Stockholders' Equity	3.6%	7.5%	4.1%	3.0%	12.3%
Continuing Operations As a % of Sales	.74%	1.50%	.66%	.44%	1.35%

Ten Year Review

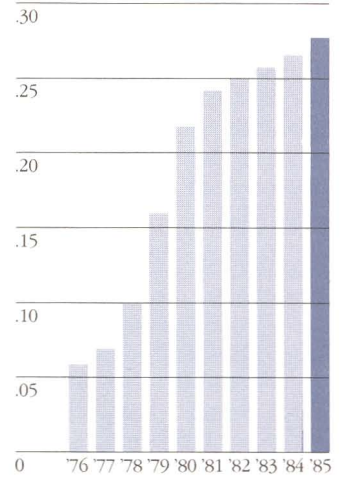
Net Income
\$ in thousands



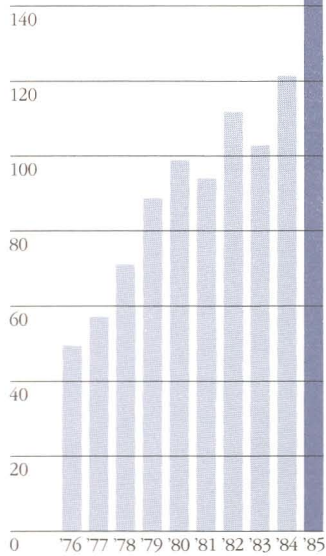
Net Income Per Share
in \$



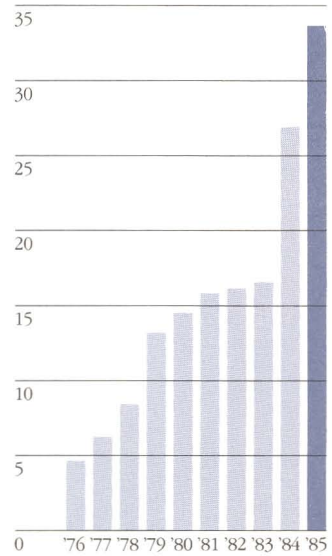
Cash Dividends Per Share
in \$



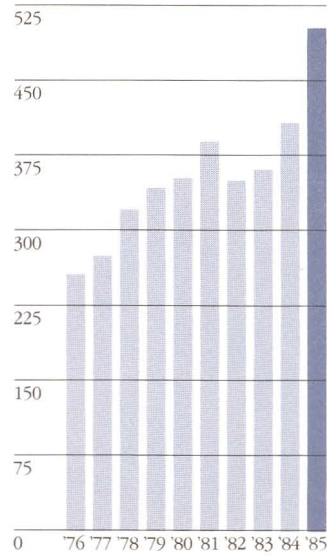
Sales
\$ in millions



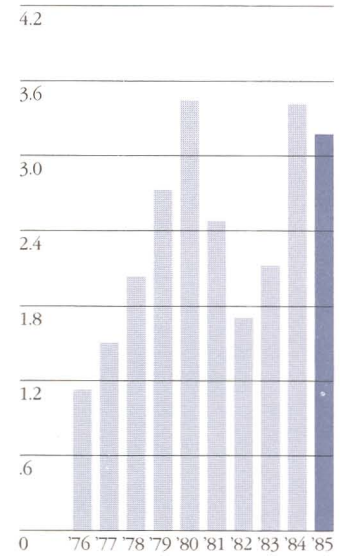
Net Worth
\$ in millions



Number of Employees



Cash Flow
\$ in millions



*Consolidated
Balance Sheets*

<i>Assets</i>	January 25, 1985 and January 27, 1984	1985	1984
Current Assets:			
Cash	\$	480,755	\$ 333,395
Receivables, less allowance for doubtful accounts of \$627,000 in 1985 and \$374,000 in 1984		16,043,144	11,910,203
Current portion of notes receivable		408,585	213,414
Inventories (Note 1)		16,358,761	15,011,766
Income tax receivable		929,451	—
Prepays		208,518	171,282
Total current assets		34,429,214	27,640,060
Land, Buildings and Equipment, at cost (Notes 1 and 3):			
Land and land improvements		2,152,551	1,759,135
Buildings		9,189,657	6,883,664
Equipment		9,764,912	8,322,964
Property held under capital leases		3,259,477	3,149,807
Furniture and fixtures		2,681,713	1,974,328
		27,048,310	22,089,898
Less-accumulated depreciation and amortization		(9,980,209)	(8,841,695)
		17,068,101	13,248,203
Other Assets:			
Notes receivable, net of current portion of \$408,585 in 1985 and \$213,414 in 1984, included in notes receivable above		992,696	959,644
Investments		738,822	425,537
Other		174,350	216,464
		1,905,868	1,601,645
		\$53,403,183	\$42,489,908

Palmer G. Lewis Co., Inc. and Subsidiaries

The accompanying notes are an integral part of these balance sheets.

<i>Liabilities and Stockholders' Equity</i>	1985	1984
Current Liabilities:		
Short-term notes payable (Note 2)	\$ 4,200,000	\$ 1,100,000
Current portion of long-term debt and obligations under capital leases	360,243	244,939
Accounts payable	7,363,552	6,704,501
Accrued salaries and wages	1,278,568	1,223,122
Other accrued liabilities	1,410,849	823,859
Income taxes payable	—	43,087
Total current liabilities	14,613,212	10,139,508
Long-Term Debt (Note 3)	2,746,974	2,351,900
Obligations Under Capital Leases (Note 3)	2,552,306	2,653,958
Less-current portion shown above	(360,243)	(244,939)
	4,939,037	4,760,919
Deferred Income Taxes (Note 4)	672,000	503,000
Minority Interest	—	57,774
Commitments (Note 5)		
Stockholders' Equity (Notes 1, 6 and 9):		
Common stock par value \$1.00—		
Authorized 8,000,000 shares;		
Issued and outstanding 3,741,025 shares in 1985		
and 2,843,598 shares in 1984	3,741,025	2,843,598
Paid-in capital	25,218,789	19,029,858
Retained earnings	4,219,120	5,203,327
	33,178,934	27,076,783
Less-treasury stock 5,258 shares in 1984 at cost	—	(48,076)
	33,178,934	27,028,707
	\$53,403,183	\$42,489,908

*Consolidated Statements
of Income*

For the three fiscal years ended January 25, 1985	1985	1984	1983
Net Sales (Note 7)	\$144,382,029	\$121,043,541	\$103,496,694
Cost and Expenses:			
Cost of goods sold	117,785,159	98,120,988	83,847,465
Selling, general and administrative expenses	22,597,446	17,990,682	15,804,263
Interest	1,345,667	982,212	1,725,351
Depreciation and amortization	2,079,614	1,598,542	1,397,418
Employees' profit sharing plan	244,427	356,874	127,274
Interest income	(488,314)	(294,167)	(281,509)
Other	(503,801)	(590,767)	(136,796)
	143,060,198	118,164,364	102,483,466
Income before provision for income taxes	1,321,831	2,879,177	1,013,228
Provision for Income Taxes (Note 4)	249,000	1,059,000	335,000
Net Income	\$ 1,072,831	\$ 1,820,177	\$ 678,228
Per Share Data (Note 1):			
Net income	\$.31	\$.67	\$.34
Dividends			
Cash	\$.28	\$.27	\$.26
Stock	4%	4%	4%

Palmer G. Lewis Co., Inc. and Subsidiaries

The accompanying notes are an integral part of these statements.

*Consolidated Statements
of Stockholders' Equity*

For the three fiscal years ended January 25, 1985

	Common Stock		Paid-in Capital	Retained Earnings	Treasury Stock	
	Shares	Amount			Shares	Amount
Balance, January 29, 1982	1,766,492	\$1,766,492	\$ 8,825,220	\$5,730,625	(4,016)	\$ (31,680)
Sale of common stock under stock purchase and stock option plans (Note 6)	9,552	9,552	28,149	—	18,016	137,180
Purchase of treasury stock	—	—	—	—	(18,000)	(143,500)
Common stock dividend	69,733	69,733	540,431	(610,165)	—	—
Cash dividends	—	—	—	(510,486)	—	—
Net income	—	—	—	678,228	—	—
Balance, January 28, 1983	1,845,777	\$1,845,777	\$ 9,393,800	\$5,288,202	(4,000)	\$ (38,000)
Sale of common stock to public	880,000	880,000	8,512,898	—	—	—
Sale of common stock under stock purchase and stock option plans (Note 6)	9,316	9,316	51,673	—	16,542	160,309
Purchase of treasury stock	—	—	—	—	(17,800)	(170,385)
Common stock dividend	108,505	108,505	1,071,487	(1,179,992)	—	—
Cash dividends	—	—	—	(725,060)	—	—
Net income	—	—	—	1,820,177	—	—
Balance, January 27, 1984	2,843,598	\$2,843,598	\$19,029,858	\$5,203,327	(5,258)	\$ (48,076)
Common stock issued for acquisition of Sea-Pac Sales Company (Note 9)	747,732	747,732	5,234,124	—	—	—
Sale of common stock under stock purchase and stock option plans (Note 6)	7,141	7,141	19,653	—	33,258	260,201
Purchase of treasury stock	—	—	—	—	(28,000)	(212,125)
Common stock dividend	142,554	142,554	935,154	(1,077,708)	—	—
Cash dividends	—	—	—	(979,330)	—	—
Net income	—	—	—	1,072,831	—	—
Balance, January 25, 1985	3,741,025	\$3,741,025	\$25,218,789	\$4,219,120	—	—

*Consolidated Statements
of Changes in Financial Position*

For the three fiscal years ended January 25, 1985	1985	1984	1983
Sources of Working Capital:			
Operations			
Net income	\$1,072,831	\$1,820,177	\$ 678,228
Charges (credits) not affecting working capital—			
Depreciation and amortization	2,079,614	1,598,542	1,397,418
Provision for deferred income taxes	169,000	61,000	9,000
Other	(172,545)	(61,862)	(35,525)
	3,148,900	3,417,857	2,049,121
Proceeds from—			
Sale of common stock	6,268,851	9,614,196	174,881
Long-term debt and obligations under capital leases	607,455	92,917	269,097
	10,025,206	13,124,970	2,493,099
Applications of Working Capital:			
Purchase of land, buildings and equipment	3,647,751	1,845,736	1,579,225
Reduction of long-term debt and obligations under capital leases	447,968	312,412	3,335,542
Cash dividends	979,330	725,060	510,486
Purchase of treasury stock	212,125	170,385	143,500
Increase in notes receivable and other, net	236,030	685,565	35,190
Net assets of acquired business, land, buildings and equipment (\$2,205,183); less long term debt (\$18,631). Excludes working capital acquired (\$5,074,366). (Note 9)	2,186,552	—	—
	7,709,756	3,739,158	5,603,943
Increase (Decrease) in Working Capital	\$2,315,450	\$9,385,812	\$(3,110,844)
Working Capital Increased (Decreased) as Follows:			
Current assets —			
Cash	\$ 147,360	\$ (468,299)	\$ 603,502
Receivables	4,132,941	600,444	2,093,586
Current portion of notes receivable	195,171	88,414	(1,743,413)
Inventories	1,346,995	2,434,219	(454,160)
Income tax receivable	929,451	—	—
Prepays	37,236	(136,754)	19,934
	6,789,154	2,518,024	519,449
Current liabilities —			
Short-term notes payable	(3,100,000)	4,250,000	100,000
Current portion of long-term debt	(115,304)	3,023,061	(2,829,000)
Accounts payable	(659,051)	(71,247)	(698,927)
Accrued salaries and wages	(55,446)	(163,828)	(418,011)
Other accrued liabilities	(586,990)	(392,148)	147,682
Income taxes payable	43,087	221,950	(265,037)
Current deferred income taxes payable	—	—	333,000
	(4,473,704)	6,867,788	(3,630,293)
Increase (Decrease) in Working Capital	\$2,315,450	\$9,385,812	\$(3,110,844)

Palmer G. Lewis Co., Inc. and Subsidiaries

The accompanying notes are an integral part of these statements.

Palmer G. Lewis Co., Inc.
and Subsidiaries
Notes to Consolidated
Financial Statements
January 25, 1985

1. Summary of Significant Accounting Policies

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of Palmer G. Lewis Co., Inc. (PGL) and its majority-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

Inventories

Inventories consist of finished goods and are primarily stated at the lower of cost, first-in, first-out (FIFO), or market. Sea-Pac states its inventory on the last-in, first-out (LIFO) method. Had the FIFO method been used, inventories would have been greater by \$1,254,000 at January 25, 1985, and \$1,242,000 at the date of acquisition.

Depreciation and Amortization, Repairs and Maintenance

Buildings, equipment and property held under capital leases are depreciated using the straight-line method over the estimated useful lives of the assets. Estimated useful lives are summarized below:

Land improvements and buildings	10-40 years
Equipment	3-10 years
Property held under capital leases	20-25 years
Furniture and fixtures	5-10 years

Maintenance, repairs and minor replacements are expensed as incurred. Betterments and replacements of major assets are capitalized. The cost and related accumulated depreciation of property sold or retired is removed from the accounts and the resultant gain or loss is reflected in operations.

Income Taxes

Deferred income taxes are provided for the reporting of items differently between financial statement and income tax purposes. Investment tax credits are recognized currently as a reduction of income tax expense.

Net Income Per Share

Net income per share is based on the weighted average number of shares of common stock outstanding during each year (3,500,174 shares in 1985, 2,719,624 shares in 1984, and 1,980,673 shares in 1983) after giving effect to the stock dividends during the years.

Profit Sharing Plan

Contributions to the Company's profit sharing plan are made at the discretion of the Board of Directors.

2. Short-Term Notes Payable

At January 25, 1985, PGL had unsecured lines of credit with banks to borrow up to \$24,000,000, primarily at prime or lower. Information regarding short-term borrowings during the three fiscal years ended 1985 follows:

<i>(Amounts in thousands)</i>	1985	1984	1983
Weighted average interest rate	11.4%	10.2%	12.9%
Average borrowings	\$7,086	\$3,175	\$6,938
Maximum amount of short-term borrowings at any monthend	13,350	9,100	10,650
Year-end short-term notes payable to banks	4,200	1,100	5,350
Year-end weighted average interest rate	9.1%	11.0%	10.5%

3. Long-Term Debt and Obligations under Capital Leases

As of January 25, 1985, and January 27, 1984, long-term debt and obligations under capital leases consisted of the following:

<i>(Amounts in thousands)</i>	1985	1984
9½% note payable to bank, secured by a mortgage on certain land and buildings, payable in monthly installments of \$3, including interest to January, 1988	\$ 282	\$ 286
8½% to 9¾% notes payable, secured by mortgages on certain land, buildings, and equipment, payable in monthly installments of \$17, including interest to 1994	1,664	1,706
10% note payable, secured by a mortgage on certain land and buildings, payable in annual installments of \$100 plus interest to July, 1989	500	—
Other (5% to 13%)	301	360
Total long-term debt	2,747	2,352
Capital lease obligations, \$31 payable monthly, including interest imputed at rates from 9% to 14½%, to 1996	2,552	2,654
Less-current portion	(360)	(245)
	\$4,939	\$4,761

The capital leases are for certain branch and office facilities. One of the leases is with a partnership in which a partner is the Chairman of the Board and a stockholder of PGL. As of January 25, 1985 and January 27, 1984, the capital lease obligation was \$1,458,000 and \$1,565,000, respectively, and the annual payments to the partnership during each of the three fiscal years ended 1985 were \$255,000. PGL may lease the facility for a term of nine more years, expiring in 1993, at the current rate or exercise an option to purchase the property at any time at fair market value. There is a renewal option at the end of the lease for an additional ten years at the then fair market value.

The following summarizes long-term debt maturities for the five fiscal years ending 1990 and subsequent years:

Fiscal Year Ending <i>(Amounts in thousands)</i>	Long-Term Debt	Capital Lease Obligations	Total
1986	\$ 221	\$ 139	\$ 360
1987	203	153	356
1988	441	849	1,290
1989	137	186	323
1990	140	205	345
Subsequent years	1,605	1,020	2,625
	\$ 2,747	\$ 2,552	\$ 5,299

4. Income Taxes

For the three fiscal years ended 1985, the provision for income taxes consisted of the following:

<i>(Amounts in thousands)</i>	Federal	State	Total
January 25, 1985			
Current taxes payable	\$ 364	\$ 42	\$ 406
Less-tax credits	(326)	—	(326)
Deferred taxes	169	—	169
Provision for income taxes	\$ 207	\$ 42	\$ 249
January 27, 1984			
Current taxes payable	\$1,090	\$ 104	\$1,194
Less-tax credits	(196)	—	(196)
Deferred taxes	61	—	61
Provision for income taxes	\$ 955	\$ 104	\$1,059
January 28, 1983			
Current taxes payable	\$ 412	\$ 33	\$ 445
Less-tax credits	(119)	—	(119)
Deferred taxes	9	—	9
Provision for income taxes	\$ 302	\$ 33	\$ 335

The tax effect of timing differences resulting in deferred income taxes for each fiscal year are as follows:

<i>(Amounts in thousands)</i>	1985	1984	1983
Depreciation	\$ 135	\$ (8)	\$ 19
Installment Sales	(8)	133	—
Retirement Benefit Plans	(54)	(18)	(10)
Capital Lease Expense	16	(15)	(20)
Accrued Vacation	17	17	17
Adjustment to LIFO reserve	56	—	—
Other-net	7	(48)	3
	\$ 169	\$ 61	\$ 9

An analysis of the differences between the effective tax rates and the Federal statutory rate is set forth below:

<i>(Amounts in thousands)</i>	1985		1984		1983	
	Amount	Percent	Amount	Percent	Amount	Percent
Federal tax at statutory rate	\$608	46.0	\$1,324	46.0	\$466	46.0
State taxes, net of Federal tax benefit	23	1.7	56	1.9	18	1.8
Investment tax credit-net	(279)	(21.1)	(155)	(5.4)	(119)	(11.7)
PAYSOP credit	(48)	(3.6)	(41)	(1.4)	—	—
Capital gains rate differential	(7)	(0.5)	(52)	(1.8)	—	—
Other-net	(48)	(3.7)	(73)	(2.5)	(30)	(3.0)
	\$249	18.8	\$1,059	36.8	\$335	33.1

5. Commitments

PGL leases certain branch facilities under "operating leases." Future minimum lease payments total \$2,699,000 and are payable as follows: 1986 \$618,000, 1987 \$544,000, 1988 \$480,000, 1989 \$477,000, 1990 \$375,000 and thereafter \$205,000. The lease obligations also extend to property taxes, insurance, and repairs and maintenance. Total lease expense charged to operations in the three fiscal years ended 1985 was \$647,000, \$545,000 and \$478,000, respectively.

6. Stock Purchase Plan and Stock Options

Stock Purchase Plan

PGL has an employee stock purchase plan for all employees with more than one year of service. Participation in the Plan is voluntary. Under the Plan, the stock purchase price is established as the lesser of 90% of the market value at the date of grant, or 100% of the market value at the date exercised, but not less than par value of \$1.00. As of January 25, 1985, 452 employees were eligible to participate in the Plan and 319 were enrolled.

A summary of the stock purchase plan activity for the three fiscal years ended 1985 follows:

Fiscal Year Ended	Shares Purchased	Average Price Per Share	Total
1985	38,172	\$7.07	\$269,900
1984	16,692	9.21	153,800
1983	22,992	6.12	140,800

At January 25, 1985, common stock reserved for issuance under this plan was 101,794 shares.

Stock Options

During the fiscal year ended 1983, the stockholders approved an Incentive Stock Option Plan retroactive to 1982, for key employees. A total of 412,650 shares of common stock has been approved for issuance under the Plan. The option price for common stock was the market value at the date of grant. The options are non-transferable and are exercisable over five years from the date of grant. As of January 25, 1985, options were granted and are outstanding to a total of 36 employees. Options for 211,050 shares of common stock were available for grant at January 25, 1985. A summary of the activity, for the three fiscal years ended 1985, follows:

	Number of Shares	Option Price		Market Price	
		Avg. Price Per Share	Total	Per Share	Total
Fiscal Year ended 1985:					
Granted	81,500	\$ 8.00	\$ 652,250		
Exercised	2,122	7.54	16,003	\$9.13	\$19,375
Outstanding and Exercisable*	200,934	7.78	1,562,600		
Fiscal Year ended 1984:					
Granted	35,500	10.00	355,000		
Exercised	8,986	7.32	65,753	10.91	98,004
Outstanding and Exercisable*	131,575	7.76	1,021,430		
Fiscal Year ended 1983:					
Granted	37,000	8.16	301,750		
Exercised	4,576	7.45	34,100	9.09	41,600
Outstanding and Exercisable*	103,772	7.14	740,700		

*Adjusted for the 4% stock dividends distributed in September 1983 and 1984.

7. Major Customer

Approximately 8%, 10% and 11% of net sales were to a major building materials retailer in the three fiscal years ended 1985.

8. Unaudited Quarterly Financial Results

<i>(Amounts in thousands except share data)</i>	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Net Sales:				
1985	\$29,082	\$40,329	\$44,308	\$30,663
1984	25,740	33,536	37,259	24,508
1983	21,795	28,581	30,832	22,289
Cost of Goods Sold:				
1985	\$23,468	\$32,892	\$36,312	\$25,113
1984	20,764	27,365	30,568	19,425
1983	17,817	23,334	25,198	17,498
Net Income:				
1985	\$ 276	\$ 497	\$ 618	\$ (319)
1984	142	554	757	366
1983	(126)	159	471	174
Net Income Per Share:*				
1985	\$.10	\$.15	\$.17	\$ (.09)
1984	.07	.20	.26	.12
1983	(.07)	.08	.24	.09

*Adjusted for Stock Dividends. Due to the averaging of common shares, quarterly net income per share may not equal the full year.

Fourth quarter adjustments and revisions to quarterly estimates (amounts in thousands):

1985 Write-down of marginal assets of approximately \$700; contribution to profit sharing plans was \$244.

Provision for income taxes decreased because of higher than expected investment tax credits and credit for payroll stock ownership plan.

1984 Contribution to the executive bonus and profit sharing plans was \$440.

Provisions for income taxes decreased because of higher than expected investment tax credits, capital gains and credit for payroll stock ownership plan.

1983 Contribution to the executive bonus and employee profit sharing plans was \$242. No contribution was made in the fiscal year ended 1982.

Provision for income taxes decreased because of higher than expected investment tax credits.

9. Acquisition

On May 16, 1984, the Company issued 747,732 shares of PGL stock plus \$1,140,384 in cash for all of the outstanding stock of Seattle Pacific Sales Company (Sea-Pac). The transaction was accounted for as a purchase and accordingly, the acquisition cost was allocated based on the fair value of Sea-Pac's net assets at May 15, 1984. Results of operations of Sea-Pac are included in the consolidated financial statements subsequent to May 15, 1984. Had Sea-Pac's results of operations been included for the full years ended January 25, 1985 and January 27, 1984, unaudited pro forma net sales and net income would have been \$153,700,000, \$151,407,000, \$929,000 and \$2,446,000, respectively.

Auditors' Report

To the Stockholders of Palmer G. Lewis Co., Inc.:

We have examined the consolidated balance sheets of Palmer G. Lewis Co., Inc. (a Washington corporation) and subsidiaries as of January 25, 1985, and January 27, 1984 and the related consolidated statements of income, stockholders' equity and changes in financial position for each of the three years in the period ended January 25, 1985. Our examinations were 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.

In our opinion, the financial statements referred to above present fairly the financial position of Palmer G. Lewis Co., Inc. and subsidiaries as of January 25, 1985, and January 27, 1984, and the results of their operations and the changes in their financial position for each of the three years in the period ended January 25, 1985, in conformity with generally accepted accounting principles applied on a consistent basis.

Seattle, Washington,
March 22, 1985.

Arthur Andersen & Co

Board of Directors

John N. Anderson
*Vice Chairman and
Chief Executive Officer*
Palmer G. Lewis Co., Inc.
Auburn, Washington

Douglas S. Gamble*^o
*President and
Chief Executive Officer*
Pacific Gamble Robinson
Seattle, Washington
(Food Distribution)

Gilbert R. Halley
*Vice President Finance
Secretary-Treasurer*
Palmer G. Lewis Co., Inc.
Auburn, Washington

J. Cutler Lewis
Executive Vice President
Palmer G. Lewis Co., Inc.
Auburn, Washington

Richard E. Lundgren†
*President and
Chief Operating Officer*
Palmer G. Lewis Co., Inc.
Auburn, Washington

Robert D. Peterson†
Chairman of the Board
Palmer G. Lewis Co., Inc.
Auburn, Washington

L.W. Wells*†^o
Executive Vice President
Winmar Company, Inc.
Seattle, Washington
(Financial Services)

Elliot K. Knutson*^o
*President and
Chief Executive Officer*
Washington Federal Savings
and Loan Association of Seattle
Seattle, Washington
(Financial Services)

*Member of Audit Committee

†Member of Executive Committee

^oCompensation Committee

Annual Meeting

The annual meeting of shareholders of Palmer G. Lewis Co., Inc. will be held on Wednesday, May 15, 1985, at 2:00 p.m. in the Auditorium of the Washington Athletic Club, 1325 6th, Seattle, Washington

Attorneys
Cartano, Botzer, Larson and Birkholz
Seattle, Washington

**Independent
Public Accountants**
Arthur Andersen & Co.
Seattle, Washington

**Registrar and
Transfer Agent**
Seattle-First National Bank
Seattle, Washington

**Additional
Information**

A copy of the Company's Form 10-K report for the year ended January 25, 1985 including financial statements and schedules, which will be filed with the Securities and Exchange Commission by April 25, 1985, is available to shareholders, without charge, upon written request to:

Gilbert R. Halley, Secretary
Palmer G. Lewis Co., Inc.
P.O. Box 1049
Auburn, Washington 98071-1049

*Management and
Service Center
Locations*

**Corporate
Headquarters**
525 C Street N.W.
Auburn, WA 98001-3944
Palmer G. Lewis
*Chairman of the Board
Emeritus*

Robert D. Peterson
Chairman of the Board
John N. Anderson
*Vice Chairman and
Chief Executive Officer*
Richard E. Lundgren
*President and Chief
Operating Officer*

J. Cutler Lewis
Executive Vice President
Gilbert R. Halley
*Vice President - Finance
Secretary-Treasurer*

Schell Harmon
*Vice President
Inventory Control*
Charles D. Lauber
*Vice President
Advertising and Promotion*
Lee R. Singer
*Assistant Treasurer
and Controller*

Louise W. Lewis
Assistant Secretary
W. Thomas Brynn
Credit Manager
John A. Fetch
Data Processing Manager
Ted C. Geocaris
National Accounts Manager
Perry W. Gorman
Personnel Manager
Carl A. Liliequist
Director of Marketing
Fred T. Poole
Marketing - Commodities

**PGL Division
Headquarters**
525 C Street N.W.
Auburn, WA 98001-3944

Jim L. Capponi
Division Manager
Dennis D. Larson
Field Sales Manager
Kenneth J. Gohrick
Inside Sales Manager
Joan E. Aliment
Credit Manager

Norman A. Larson
Trucking Supervisor
Donald R. Ray
Warehouse Supervisor

Bremerton Branch
Old Belfair Road
Bremerton, WA 98801
John C. Ruud
Manager

Marysville Branch
15102-35th Ave. N.E.
Marysville, WA 98270
Robert Dunn
Manager

Kenmore Branch
6820 N.E. 175th Street
Bothell, WA 98011
Jeffrey Z. Aiken
Manager

Spokane Branch
E. 4001 Broadway Avenue
Spokane, WA 99202
Robert E. Johnson
Manager

Wenatchee Sales Office
2717 Euclid Avenue
Wenatchee, WA 98801

Yakima Branch
2703 Fruitvale Blvd.
Yakima, WA 98902
L.L. (Pete) Briles
Manager

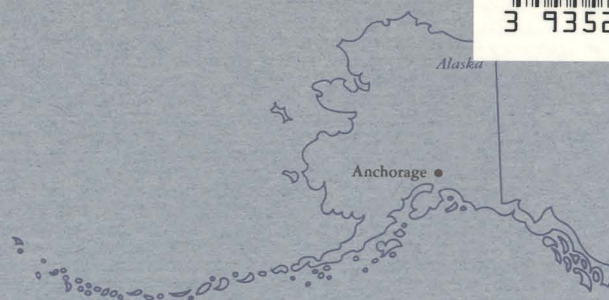
PGL Industrial Sales
233 B. Street N.W.
Auburn, WA 98002
James L. Lang
Manager

**PYS Division
Headquarters**
8100 S.W. Hunziker Road
Tigard, OR 97723

Gerald Grider
Manager
Robert R. Steen
Purchasing Manager
Margaret Taylor
Credit Manager

Medford Branch
2194 Sage Road
Medford, OR 97501
Harry Gerhard
Manager

Boise Branch
2255 Braniff Street
Boise, ID 83705
Raymond E. Ogden
Manager



Ponderosa Division

Headquarters

8435 · 24th Avenue
Sacramento, CA 95828

Earl W. Van Buskirk

Division Manager

Jerome W. Peterson

Sales Manager

Joseph M. Garfield

Purchasing Manager

N. Pat Olmstead

Administrative Manager

Anita Johnson

Credit Manager

Reno Branch

353 N. Park Street

Reno, NV 89504

Alaska Division

Headquarters

3205 Port of Tacoma Road
Tacoma, WA 98421

A. Jack Petersen

Vice President and

Division Manager

Kenneth L. Thompson

Branch Manager

Robert W. Anderson, Jr.

Inside Sales Supervisor

Harro H. Brandt

Traffic Manager

Anchorage Branch

5900 Arctic Blvd.

Anchorage, AK 99502

Richard A. York, Jr.

Manager

Sea-Pac Sales Inc.

Headquarters

3800 1st Ave. S
Seattle, WA 98134

John N. Anderson

President

Dennis R. Moore

Vice President

Resilient Division

David H. Blakley

Vice President

Appliance Division

Melvin D. Knorr

Vice President

Carpet Division

Lyman H. Black

Vice-President

Operations

Portland Branch

6060 North Cutter Circle
Portland, OR 97217-3935

Gary L. Bragg

Manager

Spokane Branch

East 410 Trent Avenue

Spokane, WA 99202

Bernice J. Beach

Manager

Billings Branch

505 N. 26th St.

Billings, MT 59101

Bernice J. Beach

Manager

Salt Lake City Branch

1011 West 2610 South

Salt Lake City, UT 84119

David G. Coleman, Jr.

Manager

Truck Service, Inc.

911 W. James Street

Kent, WA 98031

James V. Kelly

Manager

Cochrane Northwest Inc.

Headquarters

3800 1st Avenue S.

Seattle, WA 98134

Mark F. Smith

President and

General Manager

Spokane Branch

N. 110 Greene Street

Spokane, WA 98202

Boyd C. Edelin

Manager

Tacoma Branch

1916 Marc Street

Tacoma, WA 98401

Douglas Ray

Manager



Palmer G. Lewis Co., Inc.

● PGL Service Center

■ Sea-Pac Sales, Inc.

Other Operations:

Cochrane Northwest, Inc.

Tacoma

Spokane

Seattle

Truck Service Inc.

Kent

Palmer G. Lewis Co., Inc.
P.O. Box 1049
Auburn, WA 98071-1049

PGL Product Lines

Doors and Windows

Folding Doors
Marvin Terrace Doors
Marvin Wood Windows
Wood Bi-Fold Doors

Insulation Board

Armstrong Ceiling Products
Asphalt Impregnated Sheathing
Building Boards
Ceiling Grid Systems
Fiberglass and Mineral Ceilings

Lumber

1" Boards
Decking
Dimension Lumber
Glu-Lam Beams
Studs
Timbers
Treated Lumber and Plywood

Nails and Metal Products

Aluminum and Galvanized Sheets
Barbed Wire
Farm Gates
Fence Posts
Field Fence
Galvanized Merchant Wire
Galvanized Utility Fabric
Hardware Cloth
Home and Garden Fence
Horse and Paddock Fence
Livestock Water Tanks
Metal Hangers and Connectors
Nails
Poultry Netting
Rebar, Tie Wire and
Foundation Bolts
Stronghold, Helyx and Other
Specialty Nails

Plasterboard

Board Items Including
Gypsum Sheathing
Metal Trim and Metal Studs
Plasterboard Accessories
Sound Deadening Board
Vinyl Tack Board
Drywall Fasteners

Plywood

Marine Plywood
Particle Board
Plywood Sidings
Sanded and Sheathing
Special Use Plywood
Waferwood

Prefinished Wood Panels and Accessories

Prefinished Panels
Prefinished Mouldings

Rigid Insulation

Fiberboard Roof Insulation
Fiberglass Roof Insulation
Foamboard
Mineral and Urethane Insulation
Extruded Polystyrene Insulation

Roofing

Aluminum Sheets and Accessories
Asphalt Shingles and Roll Goods
Building Papers
Fiberglass Shingles and Roll Goods
Gutter Systems
Onduline Asphalt Roofing
Roof Coatings
Roof and Foundation Vents

Soft Insulation

Blanket Insulation
Household Insulation
Insulation Accessories
Sill Sealer

Specialty Products

Acrylic and Styrene Plastics
Adhesives
Bagged Concrete Products
Caulking and Sealants
Cork
Extruded Aluminum Products
Fiberglass Panels
Fireplaces
Geocel Caulking
Metalbestos Chimney Systems
Material Handling Equipment
Metal Products
Nail Bins
Olympic Stain Products
Pier Blocks
Polyethylene Film
Shower and Tub Kits
Skylights
Staplers
Tyvar Landscape Fabric
Tyvek Housewrap
Wilsonart Laminates (Reno)
Z-Brick Decorator Brick

Wallboards

Barkertile
Canfor Hardboard
Cement Board
Domestic Hardboard
Marlite Products
Trimac Melamine

Wood Shakes, Shingles and Specialty Items

Bender Board
Cedar Paneling
Peeler Cores
Railroad Ties
Shim and Undercourse Shingles
Surveyor Stakes
Wood Dowels
Wood Lath
Wood Shakes and Shingles

Sea-Pac Product Lines

Armstrong Carpeting
Armstrong Resilient Flooring
Gibson Home Appliances
Sharp Appliances

Cochrane Northwest Product Lines

Adhesives and Sealants
Cabinet and Shelf Hardware
Carpet Tackstrip
Durabeauty Laminates
Floor Tools and Accessories
Specialty Metal Trim
Staples and Specialty Nails
Vinyl Base Trim
Wilsonart Laminates