

Annual report PROFILE

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Annual Report 1990

PENWEST's strategic intent is to be a leading, innovative global marketer and manufacturer of natural polymer-based specialty chemicals and food ingredients.



## The Company

PENWEST develops, manufactures and markets specialty carbohydrate and synthetic polymer chemicals for papermaking. The company also produces and markets specialty food ingredients, agricultural nutrition supplements and pharmaceutical products.

PENWEST's principal source of revenue is Penford Products Co., the paper industry's major supplier of chemical starch coating ingredients. Penford's plants are in Cedar Rapids, Iowa, Idaho Falls, Idaho, and Richland, Washington.

PENWEST's corporate headquarters are at 777 108th Avenue NE, Suite 2390, Bellevue, WA 98004. Telephone (206) 462-6000.

### "On The Cover"

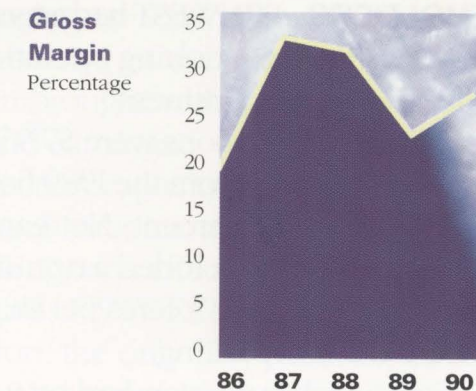
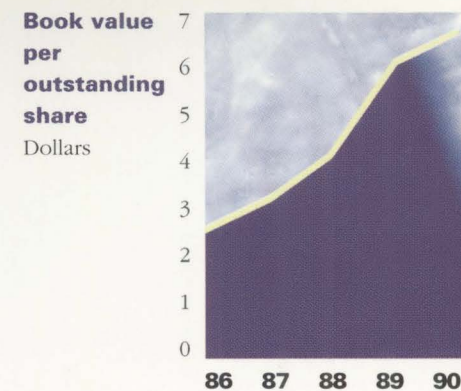
Much of what PENWEST makes and sells is all but invisible to the naked eye. But a microscope can reveal the chemist's view of things we all take for granted.

On the upper right-hand corner of the cover is a closeup, magnified 94 times, of the surface of a printing-grade sheet of lightweight coated paper of the type used in weekly news magazines.

To the eye and touch, it is smooth and featureless, but the closeup reveals an intricate structure of fibers, fillers and coatings. The chemical combination of these materials and their interrelationships on the printing press are at the heart of PENWEST's technology and product development.

In addition to presenting the financial statements, this annual report opens a microscopic window on many of PENWEST's products and the role they play in paper, foods, plant nutrients and pharmaceuticals.

The fine printing papers in this annual report have been treated with specialty starch products developed and sold through PENWEST's Penford Products Co.



## FIVE-YEAR SUMMARY

(Thousands of dollars except per share data)

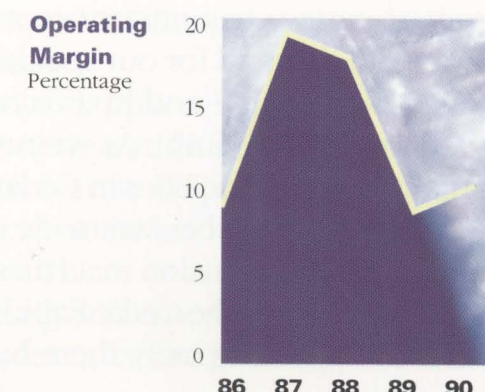
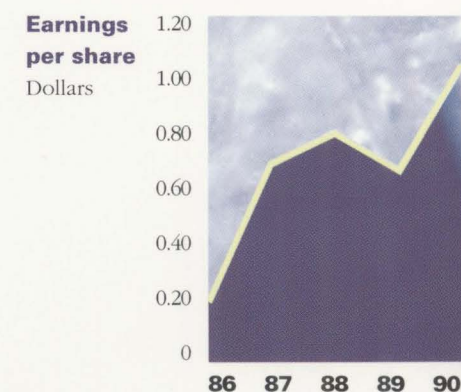
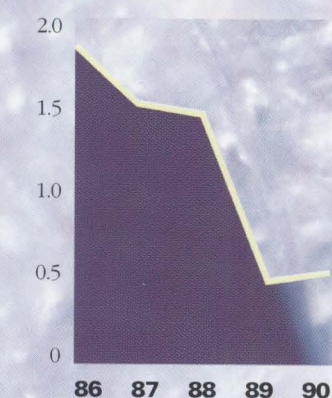
### Operating Data:

	1990	1989	1988	1987	1986
Net sales	\$ 91,998	\$ 79,826	\$ 65,819	\$ 64,004	\$ 66,671
Income from continuing operations	7,950	5,562	6,979	6,022	2,011
Earnings per share from continuing operations	1.06	0.68	0.81	0.71	0.21
Average shares outstanding	7,514,637	8,163,857	8,566,700	8,480,901	9,754,581
Effective tax rate	24.9%	29.6%	33.8%	45.2%	47.2%

### Balance Sheet Data:

	1990	1989	1988	1987	1986
Investments	30,993	38,146			
Long-term debt	23,050	23,650	49,456	39,747	45,876
Shareholders' equity	51,103	49,637	35,729	27,667	25,572
Capital expenditures	13,537	7,591	8,471	4,605	1,976
Current assets	47,977	53,582	36,085	32,623	28,790
Current liabilities	15,725	12,980	11,326	16,634	10,678
Working capital	32,252	40,602	24,759	15,989	18,012
Total assets	102,090	95,965	107,933	96,002	93,917
Total liabilities	50,987	46,328	72,204	68,335	68,345

### Interest-bearing debt to equity ratio







## LETTER TO SHAREHOLDERS

PENWEST had a terrific year. We had record earnings from continuing operations on a dramatic sales increase in our core business.

Earnings from continuing operations were \$7.95 million, or \$1.06 per share, up 43 percent from the 1989 fiscal year. Sales were \$92 million, up 15 percent. Net earnings of \$8.2 million, or \$1.09 per share, included a non-recurring fourth-quarter gain of \$264,000, or 3 cents per share, from the sale of Great Western Malting.

PENWEST's pre-tax return on operating capital, which is the standard by which we measure our financial performance, was 24 percent. Pre-tax return on financial investments was about 11 percent. Substantially all the investments represent part of the cash from the sale of Great Western Malting. The proceeds have helped fund the growth of our core business, develop new products, repay debt, repurchase stock and provide necessary capital for acquisitions. We expect to reinvest the remaining cash in operating assets over the next several years, either in acquisitions or in new products.

In addition to good bottom-line results, we launched our most important new-product innovation ever: PENGLOSS<sup>®</sup>, an exciting new coating binder, moved from the laboratory to the marketplace, and was granted a patent. Early in the first quarter of the 1991 fiscal year we began initial production runs and logged our first sales. In time, we expect PENGLOSS to be an important contributor to the company's sales and earnings, and to earn a significant share of market.

Also on the new product front, Fast Break Plus<sup>™</sup> was introduced as a line extension of Fast Break<sup>®</sup>, a timed-release nutrition supplement product for mushroom growers. Sales of these high-margin products increased 400 percent during the year, securing a significant share of their market niche.

We made important progress in reaching our goal of becoming a stronger partner to our customers. As the partnership grew, so did demand for our specialty products, most particularly our high-end hydroxyethylated starches marketed as Penford<sup>®</sup> Gum. As we neared full capacity at our manufacturing facilities in Cedar Rapids, Iowa, and Idaho Falls, Idaho, we made our third major commitment to expansion in as many years.

An \$8 million addition to the Cedar Rapids plant in fiscal 1991 will boost capacity there by 30 per-

Tod R. Hamachek  
President and Chief Executive Officer

cent, bringing to \$36 million the total expansion investment in the plant since 1988. Each expansion brought with it a corresponding increase in sales and earnings.

Production capacity in Idaho Falls, which produces potato-based cationic starches for the "wet end" of papermaking, was effectively doubled.

In April, PENWEST acquired Alpha Biochemical Corporation, the only U.S. producer of food-grade potato starches. The acquisition provides new opportunities for growth in the food ingredients business, which we have targeted as a significant PENWEST growth opportunity for the 1990s. The new business produces six food products for major U.S. consumer products companies. Potato starches enable food products to reach a smooth, creamy texture at relatively low temperatures, making them more suitable than corn



starches for microwave applications.

Other PENWEST products did well. SoluDEX<sup>®</sup>, a bulking agent for food and pharmaceutical products, now is produced in-house, making it more economical and enabling us to exercise more direct control over quality and service.

CarriDex<sup>™</sup>, a new dextrose bulking agent for low-calorie sweeteners, was introduced to the marketplace in June. Used for candy, fruit dusting and as a bulking agent, the new product supplements Cantab<sup>®</sup>, a corn sugar product which has been part of the line for a number of years.

We expect continuing gains in both volume and market share for our food ingredient products.

Without exception, all major business trends for PENWEST remain favorable as we begin the new year. Our core-business specialty chemical starch products have grown at a 25 percent rate despite cyclical paper industry sales. As total sales of paper products ease somewhat, the industry focuses greater attention on quality and production efficiency, both of which are enhanced by Penford products.

Generally soft economic trends in North America have had no visible impact on PENWEST's sales or earnings, nor, at this time, do we see any signs of a negative effect in



fiscal 1991. We expect to grow even if the paper industry, our major customer, does not.

Our plan for 1991 includes a number of priorities.

We are actively exploring the potential of PENGLOSS for selected European markets. Papermakers in Europe account for 46 percent of the estimated \$650 million western market for latex, which PENGLOSS replaces. We believe long-term opportunities in Europe are attractive, although we first must have a plant there.

In addition to geographic expansion, we are developing PENGLOSS technology for possible applications beyond the light-weight coated paper market for which it was first intended. We hope to report details later in the year.

The food products group — including bulking and tableting agents as well as the newly-acquired food-grade potato starch products — will be restructured as a separate profit center, reporting to the chief executive. We believe the realignment will help us bring greater focus to the growth opportunities in those business segments.

Because innovation is an integral part of our growth, we formalized both our commitment to and our organization for new ideas. In October 1990 Robert G. Widmaier was named Chief Innovation Officer, a new position. Bob, who holds a Ph.D. in pharmaceutical chemistry from Purdue University, joined PENWEST in 1983. In this new position, he will direct the development of new products, services, technologies and improved across-the-board efficiencies. He also will have broad responsibility for sustaining an internal culture that rewards efficiency and nurtures a spirit of change. In support of this new position, an Innovation Committee of the Board of Directors has been created. These actions recognize the fact that our company has two ways to grow: externally through acquisition, and internally through innovation. Innovation throughout the company is both an engine of change and the best path to long-term growth.

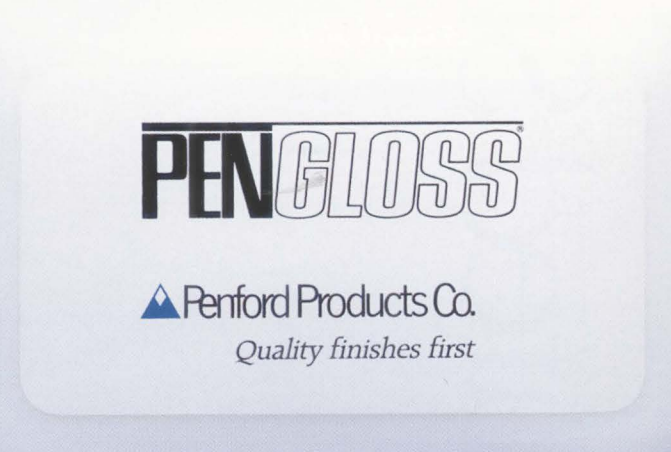
While PENWEST has been and will continue to be profitable, customer satisfaction is the principal standard against which we measure our success. Serving customers better is the driving force behind all we do. We will broaden the lines of communication with customers in 1991 as part of a continuing effort to serve their needs for greater efficiency and higher quality. In 1990 we moved our customer technical service people geographically closer to our customers' mills and strengthened their backup expertise at our Cedar Rapids facility. We continue to guarantee on-time delivery on most of what we sell. To our customers, the guarantee means added efficiency and lower inventory costs.

We continue our search for new external growth opportunities through acquisition. We review specific candidates that may offer additional markets, channels of distribution, new but related technology or product line extensions. This has been an unhurried process driven by our business needs rather than by the calendar.

Although much of our production focus in recent years has been on filling a

soaring demand for our specialty products, we continue to seek additional profit opportunities from greater efficiency. We recognized a number of employees for outstanding contribution to that effort. Two supervisory employees were cited for helping develop a process change that will make possible a 25 percent production increase in our specialty chemical starch line while saving \$1.5 million. Another employee was honored for a process change that increased output of potato starches by 33 percent at a total cost to the company of \$34. These employees exemplify the high caliber of people on PENWEST's team.

Market-driven research and development plays an increasingly key role in our long-term growth. While PENGLOSS may be the most recent and visible result of our aggressive research efforts, it is by no means the only effort. New products and service



development will remain in the forefront of our overall business strategy for two interrelated and compelling reasons: PENWEST customers increasingly rely on our technology to help them improve quality and production efficiency, and our competitive advantage in the marketplace is dependent on our leadership in technology.

Management at PENWEST is fully committed to our longstanding mission: to create the maximum continuing rate of value growth through long-term profit on invested capital and the growth of that capital. To achieve that mission we will become a leading, innovative global marketer and manufacturer of natural polymer-based, specialty chemicals and food ingredients.

A sense of the enthusiasm behind our formal mission statement was expressed in an abbreviated version recently by Jerry Turner, a millhouse operator at the Cedar Rapids plant, as he welcomed visitors to a plant tour.

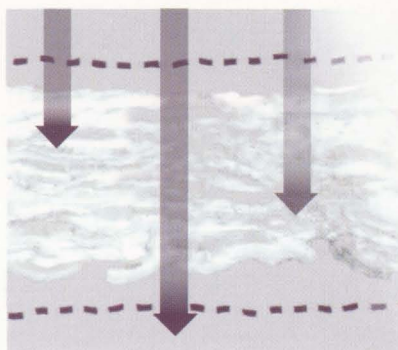
"Welcome to PENWEST," he said. "We're a great little company that's about to become awesome."

We couldn't express our own confidence any more eloquently.

Tod R. Hamachek  
President and Chief Executive Officer  
December 3, 1990



# Ethylated Starch



**POROSITY** is the relative ease with which fluids (like air or water) can pass through a sheet of paper. Porosity depends on the number and size of tiny holes in the paper and its coating, and can be measured by the rate of air flow through a sample. During printing, porosity influences how ink and fountain solution can be drained from the surface of a sheet and how fast the sheet can be dried with heat on a high-speed press. Products from Penford can increase porosity and reduce blistering.

**PAPER PRODUCTS** PENWEST's principal business is supplying specialty chemical starches and services to help papermakers improve quality and increase productivity in high-end papers for printing.

The company, through its Penford Products Co., makes and markets a full line of carbohydrate-based products that help achieve many end-product characteristics important to both papermakers and printers.

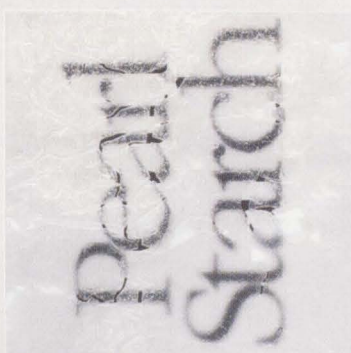


Some of the characteristics are detailed on these pages.

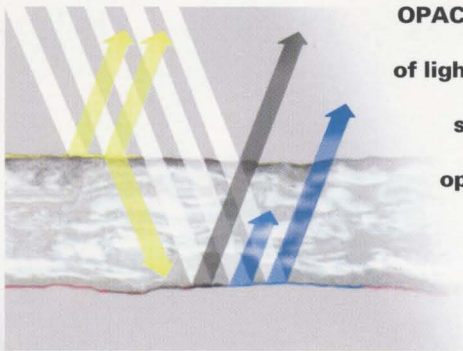
Penford products are used in three basic papermaking applications: internal bonding, for paper strength; sizing, to prepare the paper for further applications and to make it resistant to fluids; and coatings, to help printers achieve the optimal results from the printed image.

In the four-page photo above, a cross section of light-weight

**PENWEST's single greatest product success has been converting paper mills from "pearl" or commodity-type starches to highly-modified specialty hydroxyethylated starches. The difference between the two products is illustrated in this example. Pearl starches (left) can be inconsistent in coating applications, and can easily produce surfaces that are uneven and rough. Penford Gums, a line of specialty chemical starches, produces a smoother, more consistent surface for higher print quality.**





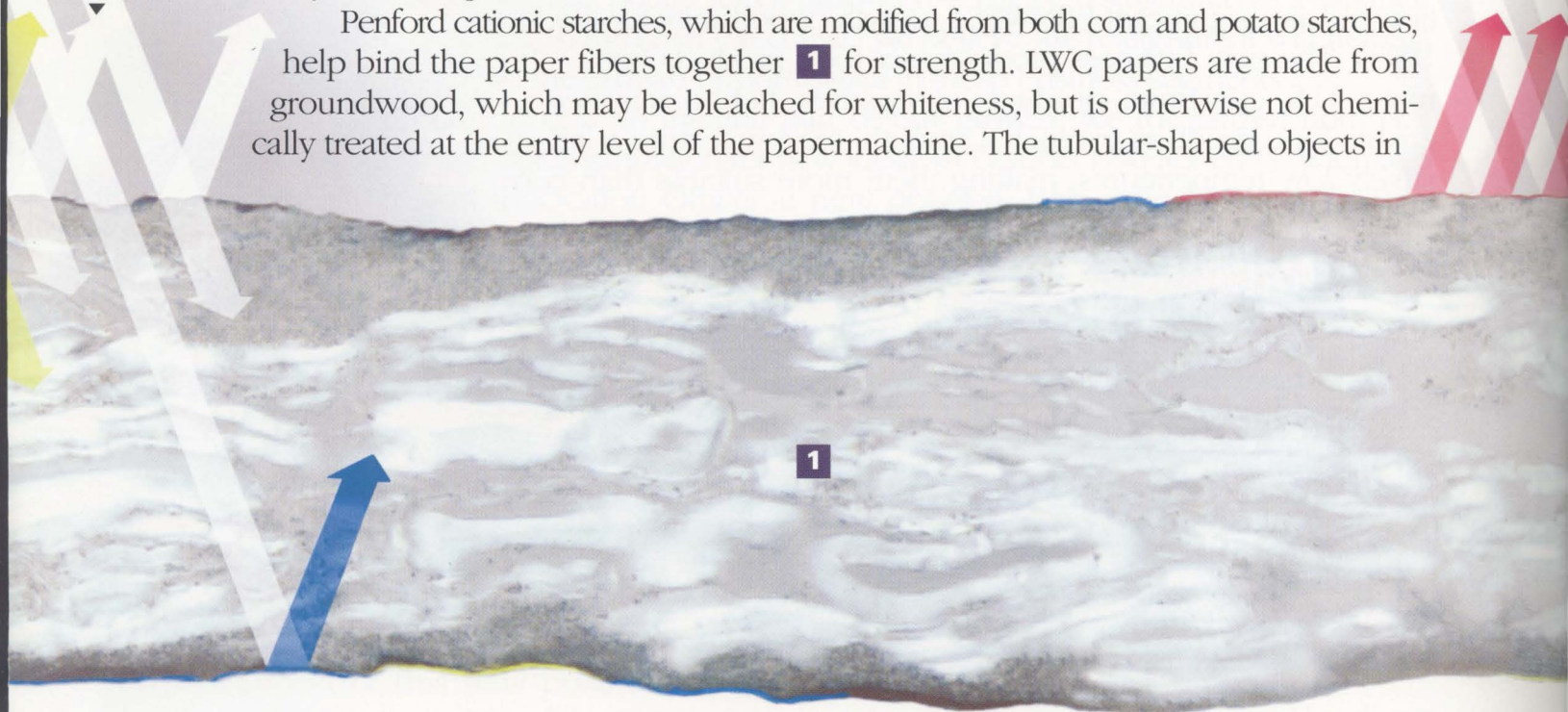


**OPACITY** is a measure of how well a sheet of paper blocks the transmission of light. It is the ratio of the relative reflectivity of a sheet backed by a black surface compared with the same area backed by a white surface. Good opacity blocks "show-through" and prevents the printing on one side of the paper from interfering with reading print on the other side.

Penford products create good structure in coatings by distributing coating materials evenly, helping to improve opacity.

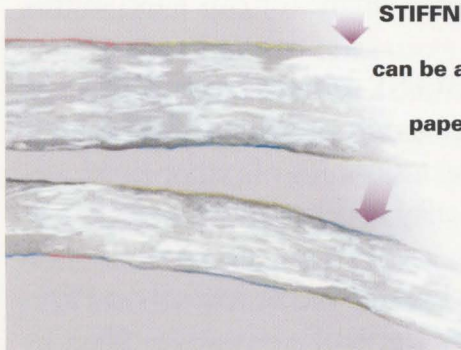
coated paper (LWC), using three Penford starch-based products, is enlarged 1,200 times by microscope.

Penford cationic starches, which are modified from both corn and potato starches, help bind the paper fibers together **1** for strength. LWC papers are made from groundwood, which may be bleached for whiteness, but is otherwise not chemically treated at the entry level of the papermachine. The tubular-shaped objects in



the cutaway are hollow cellulose fibers. During papermaking, these fibers are flattened and pressed together. As water is removed from the sheet, the fibers adhere to one another in an overlapping pattern. Cationic supplements help bridge the gap between fibers, providing additional bonding that keeps the paper in one piece during printing.

As the raw material works its way from pulp to finished product, it will be moistened and dried three times, travel at speeds of 3,000 feet per minute on the papermachine, and layered with chemicals, fillers, pigments, adhesives and coatings. Later, at the



**STIFFNESS** is partly a function of the caliper, or thickness, of the paper, but it can be augmented by coatings. Consumers regard stiffness as a component of paper quality, making it desirable, for example, in sales literature. Stiffness also is a valuable characteristic for light-weight coated papers in high-speed binderies of the kind used by magazine printers. Starch-based products from Penford promote stiffness, which is almost certain to become more important as producers shift to lighter weight paper.





**INK GLOSS** is a measure of the light reflected from the surface of an ink film printed on a sheet of paper — to the reader it appears “shiny.” Ink gloss can be affected by many things, including the chemistry of the ink itself, the interaction between the paper and the ink, ink “holdout” — which is the way the ink is displayed on the surface of the paper — and paper smoothness. Specialty Penford products can enhance ink holdout and therefore improve ink gloss.

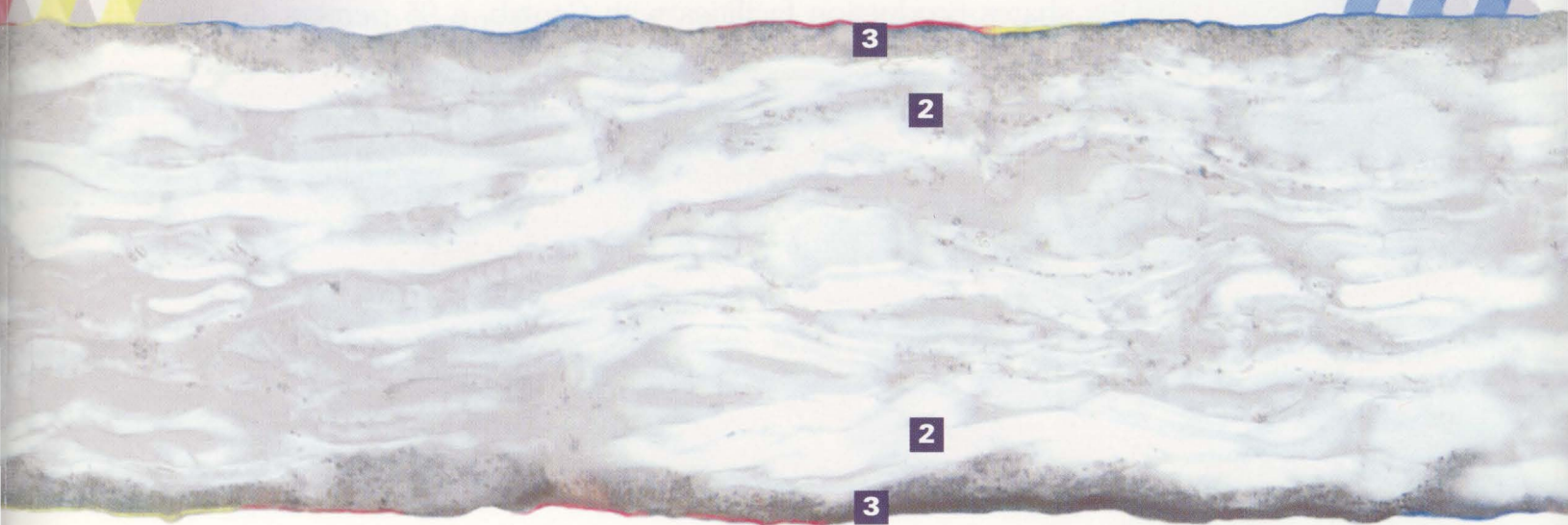
printer, the paper will pass through high-speed printing presses at 2,000 feet per minute as many as five times to receive full-color images with impact and fidelity.

Penford products play a major role in sizing **2** — sometimes a second step in the higher quality segment of the LWC manufacturing process prior to coating. Sizing is similar to applying a primer before paint. Penford Gum, a highly-modified specialty cationic starch which is not itself visible under a microscope, is the in-

Good Ink Gloss

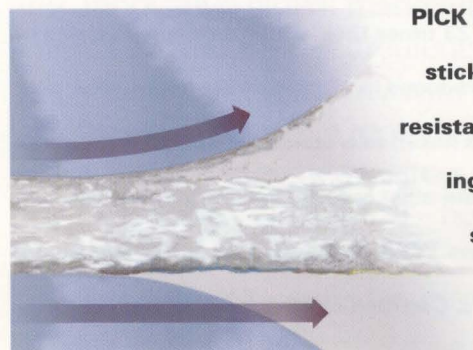
Poor Ink Snap

Good Ink Snap



dustry’s leading sizing agent. It helps smooth the surface fibers, renders the paper more resistant to water and prepares the surface for additional applications. Sizing starches comprise only about 5 percent of the paper’s bulk.

After sizing, the LWC paper receives coatings **3** which generally includes a mixture of clays, other additives and a binder — in this example a specialty starch-based binder called PENGLOSS. Eighty percent of the total coatings bulk is pigment, which gives paper its gloss and opacity. The pigment particles are held in place on the paper surface by the



**PICK RESISTANCE** describes the ability of a paper surface to withstand the sticky “pull” of an inked printing plate on a high-speed press. The relative resistance is a function of combined coating/basesheet strength. Press picking is a serious defect for a coated paper because it forces the printer to shut down and clean the press frequently or use less tacky inks which have problems of their own. In trials and in production runs, **PENGLOSS**-treated papers print cleanly without picking on the press.





**SNAP is related to both sheet gloss**

**— the shininess of the paper sur-**

**face — and ink gloss. Snap is the**

**difference between sheet gloss and**

**ink gloss after printing. It**

**describes a condition we perceive**

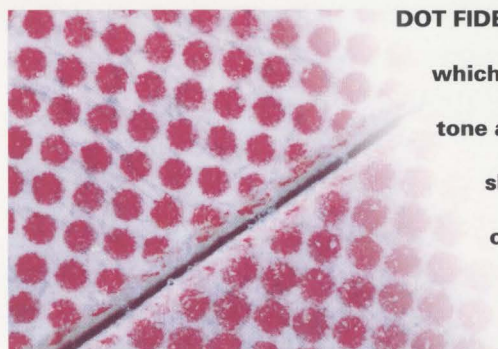
**as vivid color and high impact.**

binder. PENGLOSS, which went into commercial production early in the 1991 fiscal year, is formed by creating a chemical link between starches and — for the first time — latex binders.

PENGLOSS is a new product with major implications for PENWEST's growth. In trial runs and in commercial applications, PENGLOSS has contributed

measurably to high-quality paper production. Both papermakers and printers reported a number of improved characteristics from PENGLOSS-treated paper. Some of these characteristics are described on the accompanying displays. In addition to its use as a binder, PENGLOSS technology offers a number of other commercial opportunities now being explored by the company's research and development team.

Papermakers and printers look for many characteristics in quality papers, and specialty chemical starches from Penford Products help deliver results.



**DOT FIDELITY refers to the appearance and shape of the tiny printed circles**

**which, when combined with thousands of other tiny printed circles, give**

**tone and color to four-color offset images. Experienced printers look for**

**sharply defined dot borders and solid, uniform ink color and density**

**on the surface of the dot. Cleanly printed dots produce crisp, clean-**

**looking prints. PENGLOSS (example, top left) helps insure a clean,**

**circular edge with a solid, uniform film of surface ink.**



**FOOD PRODUCTS** PENWEST's food ingredients and pharmaceutical excipient business is targeted for significant growth in the next five years (excipients are the components of a tablet other than the active ingredients, including coating, color, binder and agents that hasten disintegration in the digestive system). These products currently account for only a relatively small portion of overall revenue, but with the introduction of new products, the acquisition of Alpha Biochemical Corporation and the company's increasing commitment to R & D and marketing, they will become a stronger contributor.

CarriDex, a new product introduced in 1990, shows particular promise. A 100 percent dextrose-based product, CarriDex can be used as a bulking agent for low calorie sweeteners, tableted candies and for meat curing. The market in which it competes is estimated at \$15 million to \$30 million.

CarriDex readily dissolves in liquids, making it especially suitable for powdered drink mixes, and its excellent flowability makes it particularly attractive for automated filling and packaging. CarriDex also is less complicated than competitive products to describe on consumer-product labels.

CarriDex shares production facilities with Cantab, a 95 percent dextrose



product that has been part of the company's food product line for many years. While CarriDex is ideal for soft candies, Cantab works best in hard candies and as a binder for tableted medicines.

Major U.S. pharmaceutical companies use Cantab for a variety of tableted products.

Cantab also is used by food producers as a "fruit dusting" for sticky foods like raisins, prunes, apricots and dates. Consumers will find Cantab in many breakfast cereals fea-



**The spheres, shown at the left at 23 times their actual size, are particles of CarriDex, a PENWEST product introduced in 1990. CarriDex competes with crystalline dextrose products (inset) as a bulking agent for low-calorie sweeteners, tableted candies and meat curing. The product is especially suited for powdered drink mixes. While both CarriDex and conventional dextrose are sugars, CarriDex compacts more readily, flows better on the production line and dissolves twice as fast in fluids.**





**PENWEST's patented SoluDex**

**(right) is magnified 23 times. It**

**contrasts with a conventional**

**maltodextrin (left). The larger**

**particle size and greater porosity**

**enable SoluDex to carry flavors**

**better and compact more easily.**

turing dried fruit. Because of its uniform particle size, Cantab flows well and creates less airborne "sugar dust" in the workplace. It competes in a \$3.5 million to \$6 million market.

SoluDex is the company's patented specialty maltodextrin product. It has a number of characteristics that give it an advantage over competitive products. It handles better, flows well and emits less "dust" in production. It is a superior tableting agent



and is highly soluble. Because of its larger particle size and high porosity, it absorbs flavors and oils better than other products.

SoluDex carries flavor in products like powdered drink mixes and coffee whiteners, can be compacted for bouillon cubes and shows potential for use in tablets. It is marketed in a segment estimated at \$6 million to \$12 million.

The acquisition of Alpha Biochemical Corporation offers PENWEST an opportunity to expand into the \$300 million food starch market. It is the only food-grade potato-starch producer in the U.S., and makes and markets six product lines under the PenPlus trademark. PenPlus products are water soluble powders used as thickeners in soft cookies, puddings, pie fillings, gravies, soups, sauces and other food products. Customers include several major U.S. food makers.

Potato starches perform better than corn starches in microwavable foods, and have a cleaner flavor. Potato starches are bland, while corn starch retains its corn flavor.

PENWEST's share of the growing U.S. modified food starch market is modest. Through aggressive marketing and innovative product development, the company believes it can increase share. Dry powdered starches for aquaculture, the fastest-growing segment of the world agricultural market, also are produced and sold through this new business.



## FINANCIAL REVIEW

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

#### Comparison of Fiscal 1990 to 1989 Results

Sales increased \$12.2 million, or 15.2 percent during 1990. Almost all of the change was additional volume, led by specialty ethylated starches.

Gross margins were 27.4 percent for 1990, up from 1989's 23 percent. Last year's gross margin was unusually low in the first half of the year because of higher drought-related raw material prices. Margins were generally stable during 1990 due to the company's policy of hedging raw material prices on fixed price sales contracts. The mix of products sold shifted to include more higher margin specialty products.

Operating expenses increased \$4.3 million, to \$15.3 million in 1990. The change relates to higher personnel costs and greater expenses in sales and research and development in anticipation of PENGLOSS®. This new product was announced in February 1990 and shipments began in the first quarter of fiscal 1991.

The company continues to invest the proceeds from the sale of Great Western Malting in a portfolio of short-term securities. Investment income was \$2.9 million compared to \$3.5 million in 1989. The decline is due to a smaller average investment portfolio in 1990. Yields were comparable between years.

Interest expense was \$700,000 less in 1990 because of lower average borrowings (\$27 million vs. \$49 million in 1989) partially offset by the allocation of interest expense to discontinued operations in 1989. The average interest rate was about one half percentage point lower in 1990.

Income tax expense was \$2.6 million at an effective rate of 24.9 percent. The effective rate is less than the statutory rate because of tax-advantaged investment income and the reversal of deferred taxes.

Income from continuing operations was \$7.95 million, an increase of 42.9 percent from 1989. Weighted average shares outstanding declined to 7.5 million, which reflected a full year's impact of the Dutch auction stock purchase completed in March 1989. A total of 1.1 million shares was purchased through the Dutch auction.

Without exception, all major business trends for PENWEST remain favorable as fiscal 1991 begins. Demand for our core business specialty chemical starch products continues to grow at a rapid rate despite cyclical paper industry sales. As total sales of paper products ease somewhat, the industry focuses greater attention on quality and production efficiency, both of which are enhanced by PENWEST products.

Generally soft economic trends in North America have had no visible impact on PENWEST's sales or earnings, nor at this time do we see any signs of a negative effect in fiscal 1991.

#### Comparison of Fiscal 1989 to 1988 Results

Sales increased \$14 million, or 21 percent during 1989. Volume at Penford Products Co. was up 10 percent with unit price increases accounting for the rest of the change. Price increases reflected the impact caused by the 1988 drought and its impact on raw materials prices.

Gross margins declined from 31.7 percent to 23 percent because of higher raw materials costs resulting from the drought. This problem was alleviated by the end of the second quarter as the contracts were renegotiated and margins returned to a more normal level in the last two quarters of the year.

Operating expenses increased \$2 million, or 22.6 percent during 1989. The company increased expenditures for research and development for new products and acquisition searches.

Proceeds from the sale of Great Western Malting Co. were invested in short-term instruments. Investment income was \$3.5 million; there was no investment income in 1988.

Interest expense doubled in 1989 to \$2.9 million. The expense is ahead of last year's amount because interest was no longer partially allocated to discontinued operations. The allocation was based on net tangible assets employed.

Income tax expense was \$2.3 million at an effective rate of 29.6 percent. PENWEST's rate is less than the statutory rate because of tax-advantaged investment income and the reversal of deferred taxes.

Income from continuing operations was \$5.6 million, down \$1.4 million from 1988. Earnings per share were \$0.68 against \$0.81 in 1988. The weighted average shares outstanding declined to 8.2 million from 8.6 million due to the impact of the Dutch auction completed in March.



## Liquidity and Capital Resources

PENWEST is in a highly liquid position as a result of the 1989 Great Western sale. About 30 percent of our assets are in short-term investments. In addition, the company has a three-year, \$25 million revolving credit agreement. At year-end, there were no outstanding borrowings under this agreement.

A new borrowing of \$6 million was completed in December 1989. These funds were used to acquire 341,254 shares of PENWEST common stock in the open market which were in turn sold to the PENWEST Savings and Stock Ownership Plan. Subsequent to year-end, \$4.3 million of mortgages matured and were repaid with an equivalent new borrowing. The two completed borrowings will bear interest at 9.7 percent because the interest rate was hedged in 1989. The company has \$17.7 million of anticipatory hedges outstanding after giving effect to these two new borrowings.

The company anticipates completing a \$22 million term debt borrowing with a group of banks during the first quarter of fiscal 1991. The proceeds will be applied to borrowings outstanding under uncommitted lines of credit.

Operating cash flow was \$10.4 million, \$11.9 million and \$1.4 million in 1990, 1989 and 1988 respectively. The decline in 1990 was due to an increase in working capital.

Capital expenditures rose to \$13.5 million from \$7.6 million in 1989. Expenditures have been funded from operations and, when necessary, temporary borrowings under the uncommitted lines. The largest projects were the new PENGLOSS® manufacturing plant, corn grind expansion and a chemical storage complex. Capital expenditures in fiscal 1991 will at least be at the 1990 level and will be funded from operations and borrowings, if necessary. The \$22 million term debt borrowing referred to above will fund 1990 and 1989 capital expenditures on a long-term basis.

Expansions completed in 1989 enabled us to meet the growing demand for specialty ethylated starches. Capital projects in fiscal 1991 will include additional treating and drying capacity to meet future sales demand, as well as the completion of projects started in the prior year. The PENGLOSS facility came on line in the first quarter of fiscal 1991 and did not contribute to sales in 1990.

A 50 percent stock dividend was paid during the year. This had no impact on liquidity; however, the company expects that the resulting lower price will maintain the stock in an affordable trading range. The Board of Directors reviews the dividend policy on an annual basis.

Other long-term assets increased \$3.7 million. On September 1, 1989, PENWEST adopted pension accounting changes which resulted in an asset of \$2.2 million being included in this caption. The remainder of the increase represents the purchase of company-owned life insurance.

In December 1987, the Financial Accounting Standards Board issued Statement No. 96 "Accounting for Income Taxes," adopting the liability method of accounting for deferred income taxes. Statement No. 96 must be adopted by PENWEST no later than the fiscal year ending August 31, 1993. Deferred taxes will be adjusted to reflect federal income tax rates in effect at the time of adoption. Based on current tax rates, the benefit from adoption at August 31, 1990 would be approximately \$1.6 million. The company intends to adopt Statement No. 96 in fiscal 1993.



## CONSOLIDATED STATEMENTS OF INCOME

(Thousands of dollars)	Year Ended August 31		
	1990	1989	1988
Sales	\$91,998	\$79,826	\$65,819
Cost of sales	<u>66,830</u>	<u>61,502</u>	<u>44,980</u>
Gross margin	25,168	18,324	20,839
Operating expenses	<u>15,277</u>	<u>10,957</u>	<u>8,939</u>
Income from operations	9,891	7,367	11,900
Investment income	2,899	3,463	
Interest expense	<u>(2,203)</u>	<u>(2,935)</u>	<u>(1,352)</u>
Income from continuing operations, before taxes	10,587	7,895	10,548
Income taxes	<u>2,637</u>	<u>2,333</u>	<u>3,569</u>
Income from continuing operations	7,950	5,562	6,979
Income from discontinued operations:			
Operating results, net		5,344	2,566
Gain on sale, net	<u>264</u>	<u>22,404</u>	<u></u>
	264	27,748	2,566
Net income	<u>\$ 8,214</u>	<u>\$33,310</u>	<u>\$ 9,545</u>
<b>Earnings per common share:</b>			
Continuing operations	\$ 1.06	\$ 0.68	\$ 0.81
Discontinued operations:			
Operating results, net		0.65	0.30
Gain on sale	<u>0.03</u>	<u>2.75</u>	<u></u>
	0.03	3.40	0.30
	<u>\$ 1.09</u>	<u>\$ 4.08</u>	<u>\$ 1.11</u>
<b>Weighted average common shares outstanding</b>	<u>7,514,637</u>	<u>8,163,857</u>	<u>8,566,700</u>

The accompanying notes are an integral part of these statements.



## CONSOLIDATED BALANCE SHEETS

August 31 (Thousands of dollars)

1990

1989

### Assets

#### Current assets:

Cash	\$ 306	\$ 625
Investments	30,993	38,146
Trade accounts receivable	8,623	7,940
Inventories	5,990	5,788
Prepaid expenses and other	2,065	1,083
Total current assets	47,977	53,582

#### Property, plant and equipment:

Land	1,248	1,137
Plant and equipment	88,033	74,752
Less accumulated depreciation	39,273	33,879
Net property, plant and equipment	50,008	42,010
Other assets	4,105	373
	<u>\$102,090</u>	<u>\$ 95,965</u>

### Liabilities and shareholders' equity

#### Current liabilities:

Accounts payable	\$ 8,127	\$ 7,044
Current portion of long-term debt	4,600	493
Accrued liabilities	2,998	5,443
Total current liabilities	15,725	12,980
Long-term debt	23,050	23,650
Deferred income taxes and other	12,212	9,698

#### Shareholders' equity:

Common stock, par value \$1.00 per share, authorized 29,000,000 shares, issued 8,494,627 in 1990 and 5,638,849 in 1989	8,495	5,639
Additional paid-in capital	12,028	11,935
Retained earnings	58,273	53,064
Treasury stock, at cost, 1,399,255 shares in 1990 and 925,240 shares in 1989	(21,600)	(21,001)
Note receivable from PENWEST Savings and Stock Ownership Plan	(6,093)	
Total shareholders' equity	<u>51,103</u>	<u>49,637</u>
	<u>\$102,090</u>	<u>\$ 95,965</u>

The accompanying notes are an integral part of these statements.



## CONSOLIDATED STATEMENTS OF CASH FLOWS

(Thousands of dollars)	Year Ended August 31		
	1990	1989	1988
<b>Operating Activities:</b>			
Income from continuing operations	\$ 7,950	\$ 5,562	\$ 6,979
Adjustments to reconcile income from continuing operations to net cash from (used by) continuing operations:			
Depreciation	5,520	4,902	4,284
Deferred income taxes	102	(722)	(416)
Other	(200)	(169)	63
Change in assets and liabilities:			
Receivables	(683)	(636)	(1,530)
Inventories	(202)	333	(2,190)
Other current assets	(982)	(655)	34
Accounts payable and other current liabilities	(1,098)	3,333	(5,838)
	<u>10,407</u>	<u>11,948</u>	<u>1,386</u>
Income from discontinued operations	264	27,748	2,566
Gain on sale of discontinued operations, net	(264)	(22,404)	
Adjustments to reconcile income from discontinued operations to net cash from (used by) discontinued operations		553	(5,649)
		<u>5,897</u>	<u>(3,083)</u>
Net cash from (used by) operating activities	<u>10,407</u>	<u>17,845</u>	<u>(1,697)</u>
<b>Investing Activities:</b>			
Additions to plant and equipment	(13,537)	(7,591)	(8,471)
Proceeds from sale of discontinued operations		76,000	
Other	19	90	32
Net cash from (used by) investing activities	<u>(13,518)</u>	<u>68,499</u>	<u>(8,439)</u>
<b>Financing Activities:</b>			
Proceeds from long-term debt	17,775	10,575	12,875
Payments on long-term debt	(14,268)	(38,947)	(2,636)
Purchase of treasury stock	(6,599)	(19,600)	(1,401)
Purchase of officers' life insurance	(1,120)		
Other	(149)	198	(82)
Net cash from (used by) financing activities	<u>(4,361)</u>	<u>(47,774)</u>	<u>8,756</u>
Net increase (decrease) in cash and equivalents	<u>(7,472)</u>	<u>38,570</u>	<u>(1,380)</u>
Cash and cash equivalents at beginning of year	<u>38,771</u>	<u>201</u>	<u>1,581</u>
Cash and cash equivalents at end of year	<u>\$31,299</u>	<u>\$38,771</u>	<u>\$ 201</u>
<b>Supplemental disclosure of cash flow information</b>			
Cash paid during the year for:			
Interest (net of capitalized interest)	\$ 2,168	\$ 4,476	\$ 3,950
Income taxes	4,682	28,826	11,983

The accompanying notes are an integral part of these statements.



## CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(Thousands of dollars)	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Note Receiv- able from PENWEST Savings and Stock Own- ership Plan	Total Share- holders' Equity
<b>Balances, September 1, 1987:</b>	\$5,591	\$11,729	\$10,347			\$27,667
Net income			9,545			9,545
Exercise of stock options	24	32				56
Redemption of shareholders' rights			(138)			(138)
Purchase of treasury stock				\$ (1,401)		(1,401)
<b>Balances, August 31, 1988:</b>	5,615	11,761	19,754	(1,401)		35,729
Net income			33,310			33,310
Exercise of stock options	24	174				198
Purchase of treasury stock				(19,600)		(19,600)
<b>Balances, August 31, 1989:</b>	5,639	11,935	53,064	(21,001)		49,637
Net income			8,214			8,214
Exercise of stock options	35	93				128
Purchase of treasury stock				(6,599)		(6,599)
PENWEST Savings and Stock Ownership Plan activity				6,000	\$(6,093)	(93)
Three-for-two stock split	2,821		(2,822)			(1)
Pension plan minimum liability			(183)			(183)
<b>Balances, August 31, 1990:</b>	<u>\$8,495</u>	<u>\$12,028</u>	<u>\$58,273</u>	<u>\$(21,600)</u>	<u>\$(6,093)</u>	<u>\$51,103</u>

The accompanying notes are an integral part of these statements.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### Note A

#### Summary of Significant Accounting Policies

##### Consolidation

The consolidated financial statements include PENWEST and its wholly-owned subsidiaries. Material intercompany balances and transactions have been eliminated.

##### Cash

PENWEST's cash management system operates so that a cash overdraft for uncleared checks exists in the disbursing accounts. Cash in the accompanying balance sheets represent amounts to be transferred to the disbursing accounts. Uncleared checks of \$2,244,000 and \$1,870,000 are included in accounts payable at August 31, 1990 and 1989, respectively.

##### Investments

Investments are carried at cost, consist of preferred stock and commercial paper and are considered to be cash equivalents. The market value of the portfolio approximates cost.

##### Property, Plant and Equipment

Property, plant and equipment are recorded at cost. Expenditures for maintenance and repairs are expensed as incurred. The company uses the straight-line method to compute depreciation for financial reporting purposes. For income tax purposes, the company generally uses accelerated depreciation methods.

Interest is capitalized on major construction projects while in progress. For continuing operations, interest of \$363,000, \$300,000 and \$158,000 was capitalized during the fiscal years ended August 31, 1990, 1989 and 1988, respectively.



### Income Taxes

Deferred income taxes are provided on timing differences between financial and income tax reporting methods.

### Earnings Per Share

Earnings per common share were computed by dividing net income by the weighted average number of common shares and dilutive common share equivalents outstanding during the fiscal year. Outstanding stock options are considered to be common share equivalents.

### Segment Information

PENWEST's primary business segment is developing, manufacturing and marketing specialty carbohydrate and synthetic polymer chemicals for papermaking. No single customer accounts for more than 10 percent of sales.

### Research and Development

Research and development costs of \$2,393,000, \$1,863,000 and \$1,342,000 in 1990, 1989 and 1988, respectively, were charged to expense as incurred.

### Reclassification

Certain prior year amounts have been reclassified to conform with current year presentation.

### Note B

#### Inventories

Inventories and deferred gains and losses from hedging transactions are stated at the lower of cost or market. Cost, which includes material, labor and manufacturing overhead costs, is determined by the first-in, first-out (FIFO) method.

The company generally follows a policy of hedging corn purchases related to fixed price sales contracts to minimize risk due to market fluctuations. Gains and losses from these hedging transactions are deferred and included in inventory until such time as the corn is converted to finished goods and sold.

Inventories consist of:

August 31 (Thousands of dollars)	1990	1989
Raw materials, supplies and other	\$ 2,829	\$ 2,744
Work in progress	433	385
Finished goods	2,728	2,659
Total inventories	<u>\$ 5,990</u>	<u>\$ 5,788</u>

### Note C

#### Long-term Debt and Revolving Credit Agreement

The long-term debt of PENWEST and its subsidiaries is as follows:

August 31 (Thousands of dollars)	1990	1989
Borrowings under unsecured lines of credit	\$17,500	\$19,350
9.55 percent unsecured note, due in quarterly installments through 2000	5,850	
8.75 percent mortgages, three of which matured in December, 1989 and three of which are quarterly interest-only payments, with final maturity in October, 1990	4,300	4,793
	<u>27,650</u>	<u>24,143</u>
Less current portion	4,600	493
Net long-term debt	<u>\$23,050</u>	<u>\$23,650</u>

The 8.75 percent mortgages were refinanced in October 1990 upon maturity.

Maturities of long-term debt and the revolving credit agreement for the fiscal years ending August 31, 1991 through 1995 are as follows (thousands of dollars):

1991	\$ 4,600
1992	300
1993	17,850
1994	450
1995	670



The company has an unsecured revolving line of credit of \$25 million with four banks which expires on April 15, 1993. Borrowing rates available to the company under the revolver are at prime rate or less depending on the selection of borrowing options. PENWEST can elect to borrow under several options, including prime, certificate of deposit, Eurodollar and bankers' acceptance rates. Borrowings under the revolving credit agreement can be converted, at the option of PENWEST, to term notes due on the expiration date of the revolving credit agreement.

The revolving credit agreement includes, among other terms, various limitations on long-term indebtedness, minimum net worth and working capital ratios, and restrictions on PENWEST's ability to purchase or redeem its own stock. Under the most restrictive of these terms net worth at August 31, 1990, must be at least \$24,107,000. The term of this agreement is extended for an additional year on an annual basis unless the commitments are withdrawn. If any bank withdraws, reduction of its commitment can be accomplished in four equal quarterly reductions commencing approximately one year after notice of election to withdraw.

The company has uncommitted lines of credit which provide for financing at various floating rates. Since this debt can be refinanced through the revolving credit agreement, it is classified as long-term.

The company sold \$28 million of Treasury note futures in August 1989 to hedge the interest rate risk of anticipated long-term borrowings. At August 31, 1990, \$22 million of the futures are outstanding and will be applied to future borrowings. The cost of the hedge is deferred and will be recognized as a component of interest expense over the life of the debt.

#### Note D

##### Stock Options

Under stock option plans, options have been granted to certain officers and key employees to purchase PENWEST common stock. Changes in stock options for the three years ended August 31, 1990 are as follows:

	1990	1989	1988	1990 Option Price Range
Outstanding at beginning of year	798,971	831,186	873,900	\$ 2.08 - 12.75
Granted	52,000		109,995	16.59 - 31.00
Exercised	(37,020)	(30,415)	(42,114)	2.08 - 5.83
Cancelled	(100,244)	(1,800)	(110,595)	5.83 - 8.83
Outstanding at end of year	<u>713,707</u>	<u>798,971</u>	<u>831,186</u>	<u>\$ 2.08 - 31.00</u>
Exercisable at end of year	<u>92,917</u>	<u>100,592</u>	<u>72,447</u>	<u>\$ 2.08 - 12.75</u>

At August 31, 1990, 76,227 stock appreciation rights (SARs) were outstanding to certain officers under related stock option grants. The SARs were granted in December 1986 and April 1988 at the market price of PENWEST stock. As a result of appreciation and vesting of the SARs \$550,000, \$230,000 and \$30,000 was charged to expense in 1990, 1989 and 1988, respectively. The SARs vest over a five-year period from the date of grant.



## Note E

### Stock Split

On February 6, 1990, the Board of Directors declared a three-for-two split of the company's common stock to shareholders of record on February 21, 1990. This stock split was effected in the form of a 50 percent stock dividend by the distribution of one additional share for each two shares of stock outstanding. The par value of the common stock remained at \$1.00 per share. As a result, \$2.8 million, representing the total par value of new shares issued, was transferred from retained earnings to common stock. Amounts per share and numbers of common shares have been restated to give retroactive effect to the stock split.

## Note F

### Income Taxes

Income tax expense consists of the following:

(Thousands of dollars)	Year Ended August 31		
	1990	1989	1988
Current			
Federal	\$ 2,348	\$ 2,772	\$ 3,765
State	187	283	220
	<u>2,535</u>	<u>3,055</u>	<u>3,985</u>
Deferred			
Federal	100	(700)	(400)
State	2	(22)	(16)
	<u>102</u>	<u>(722)</u>	<u>(416)</u>
Total provision	<u>\$ 2,637</u>	<u>\$ 2,333</u>	<u>\$ 3,569</u>

The sources of timing differences resulting in deferred income taxes and the tax effect of each consisted of the following:

(Thousands of dollars)	Year Ended August 31		
	1990	1989	1988
Depreciation	(234)	\$ (944)	\$ (730)
Other	336	222	314
Total deferred provision	<u>102</u>	<u>\$ (722)</u>	<u>\$ (416)</u>

Reconciliation of the statutory federal tax to the actual provision is as follows:

(Thousands of dollars)	Year Ended August 31		
	1990	1989	1988
Statutory rate	34%	34%	34%
Statutory tax	\$ 3,600	\$ 2,684	\$ 3,586
State income taxes, net of federal tax benefit	123	186	180
Timing differences reversing at non-originating rate	(136)	(350)	(186)
Non-taxable investment income	(664)	(313)	
Other	(286)	126	(11)
Total provision	<u>\$ 2,637</u>	<u>\$ 2,333</u>	<u>\$ 3,569</u>

### FASB No. 96

In December 1987, the FASB issued Statement No. 96 "Accounting for Income Taxes," adopting the liability method of accounting for deferred income taxes. Statement No. 96 must be adopted by PENWEST no later than the fiscal year ending August 31, 1993. Under the provisions of Statement No. 96, PENWEST may recognize the impacts of adoption by recording the prior years' cumulative effect of the new rules entirely in the year of adoption or by restating all financial statements presented. Deferred taxes will be adjusted to reflect federal income tax rates in effect at the time of adoption. Based on current tax rates, the benefit from adoption at August 31, 1990 would be approximately \$1.6 million.



## Note G

### Pension and Other Employee Benefits

PENWEST maintains two pension plans that cover substantially all employees in noncontributory defined benefit pension plans.

Benefits under the plan for hourly employees are primarily related to years of service. Benefits for salaried employees are primarily related to years of credited service and final average five-year earnings. Employees generally become eligible to participate in the plans after attaining age 21 and benefits normally become vested after five years of credited service.

The company's funding policy is to contribute amounts to the plans sufficient to meet or exceed the minimum requirements of the Employee Retirement Income Security Act. Effective September 1, 1989, PENWEST adopted the balance sheet reporting provisions of Statement of Financial Accounting Standards No. 87, "Employers' Accounting for Pensions," for both pension plans. This statement requires the recognition of an additional pension liability (included in deferred liabilities) and intangible asset (included in other assets) of \$2,159,000 and \$1,881,000, respectively, as of August 31, 1990, with a direct reduction in shareholders' equity of \$278,000 less a related tax benefit of \$95,000.

Net periodic pension expense consisted of the following (in thousands):

	Year Ended August 31,		
	1990	1989	1988
Service cost of benefits earned during the year	\$ 276	\$ 269	\$ 243
Interest cost on projected benefit obligation	1,024	1,003	1,026
Actual return on plan assets	123	(1,646)	326
Net amortization and deferral	(744)	1,139	(893)
Net pension expense	<u>\$ 679</u>	<u>\$ 765</u>	<u>\$ 702</u>

Assumptions used in the accounting for pension plan expense in 1990, 1989 and 1988 included a discount rate of 8.12 percent, 9.06 percent and 9.59 percent, respectively, a rate of increase in compensation levels of 6 percent for the salaried employees, and an expected long-term rate of return on plan assets of 8 percent.

The following table sets forth the funded status of both pension plans as of August 31, 1990 and 1989 (in thousands):

	Plans with an Obligation in Excess of Assets August 31,	
	1990	1989
Actuarial present value of projected obligation, based on service to date and current salary levels:		
Vested	\$ 11,182	\$ 12,128
Nonvested	152	135
Accumulated benefit obligation	11,334	12,263
Effect of projected salary increases	800	781
Projected benefit obligation	12,134	13,044
Plan assets at fair market value	10,359	10,134
Projected benefit obligation greater than plan assets	(1,775)	(2,910)
Unrecognized actuarial net loss	554	986
Balance of unrecognized net obligation at transition being amortized over 15 years	1,773	1,901
Unrecognized prior service cost	281	212
Adjustment to record minimum liability	(2,159)	
Net pension asset (liability)	<u>\$ (1,326)</u>	<u>\$ 189</u>

Assets of the pension plans are invested in units of common trust funds managed by Frank Russell Trust Company. The common trust funds own stocks, bonds and real estate.



#### **PENWEST Savings and Stock Ownership Plan**

The company has a savings investment plan, available to all employees, whereby it matches 75 percent of the employee's contribution up to 6 percent of the employee's pay. The match is made in PENWEST common stock. The plan held 334,452 unallocated shares of PENWEST common stock as of August 31, 1990 including shares earned but not yet allocated. During 1990, approximately 24,000 shares of stock were earned by plan participants. The expense of the plan was \$517,000, \$162,000 and \$100,000 for the fiscal years 1990, 1989 and 1988, respectively.

The plan acquired the PENWEST common stock by issuing a note to the company. The note is amortized by the release of stock to participants in the plan.

#### **Supplemental Executive Retirement Plan**

The company has a Supplemental Executive Retirement Plan (SERP) which covers certain employees. The plan is nonqualified and is subject to the provisions of Statement of Financial Accounting Standards No. 87, "Employers' Accounting for Pensions." The SERP began on September 1, 1989, and net pension expense of the SERP for 1990 was \$256,000.

#### **Note H**

##### **Shareholders' Equity**

##### **Unissued Preferred Stock**

There are 1,000,000 shares of \$1.00 par value preferred stock authorized for issue; however, none are outstanding.

##### **Common Stock Purchase Rights**

On June 16, 1988, PENWEST distributed a dividend of one right ("Right") for each outstanding share of PENWEST common stock. In addition, previously outstanding Rights were redeemed for \$0.025 each. When exercisable, each Right will entitle its holder to buy one share of PENWEST's stock at \$44.00 per share. The Rights will become exercisable if a purchaser acquires 20 percent of PENWEST's common stock or makes an offer to acquire common stock. In the event that a purchaser acquires 20 percent of the common stock of PENWEST, each Right shall entitle the holder, other than the acquirer, to purchase one share of common stock of PENWEST for one half of the market price of the common stock. In the event that PENWEST is acquired in a merger or transfers 50 percent or more of its assets or earnings to any one entity, each Right entitles the holder to purchase common stock of the surviving or purchasing company having a market value of twice the exercise price of the Right. The Rights may be redeemed by PENWEST at a price of \$.01 per Right and they expire in June, 1998.

#### **Note I**

##### **Sale of Great Western Malting Co.**

On March 13, 1989, the company sold the operating assets of the Great Western Malting Co. division. In addition, PENWEST was reimbursed for the working capital employed at Great Western.

Net sales of Great Western Malting Co. for the period ended March 13, 1989 were \$53,305,000, and for the year ended August 31, 1988 were \$82,404,000. Interest expense was \$1,740,000 and \$2,633,000 in 1989 and 1988, respectively. Interest expense was allocated on the basis of net tangible assets employed as of the beginning of the fiscal year.

Tax expense for discontinued operations for the years ended August 31, 1989 and 1988 was \$3,029,000 and \$1,312,000, respectively. Tax expense associated with the gain on the sale of the property, plant and equipment was \$9,761,000. Contingencies, if any, remaining from the sale will not be material. Reserves associated with the sale were decreased by \$400,000 less applicable taxes of \$136,000 during 1990.



**Note J****Quarterly Financial Data (Unaudited)**

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
<b>1989/90</b> (Thousands of dollars except earnings per share data)					
Sales	\$20,915	\$21,910	\$24,346	\$24,827	\$91,998
Gross margin	5,404	5,925	7,227	6,612	25,168
Income from continuing operations	1,762	1,963	2,252	1,973	7,950
Income from discontinued operations				264	264
Net income	<u>\$ 1,762</u>	<u>\$ 1,963</u>	<u>\$ 2,252</u>	<u>\$ 2,237</u>	<u>\$ 8,214</u>
Earnings per common share:					
Continuing operations	\$ 0.24	\$ 0.26	\$ 0.30	\$ 0.26	\$ 1.06
Discontinued operations				0.03	0.03
	<u>\$ 0.24</u>	<u>\$ 0.26</u>	<u>\$ 0.30</u>	<u>\$ 0.29</u>	<u>\$ 1.09</u>
<b>1988/89</b> (Thousands of dollars except earnings per share data)					
Sales	\$18,377	\$19,627	\$22,091	\$19,731	\$79,826
Gross margin	4,307	3,536	5,753	4,728	18,324
Income from continuing operations	855	525	2,310	1,872	5,562
Income from discontinued operations	2,450	2,622	22,676		27,748
Net income	<u>\$ 3,305</u>	<u>\$ 3,147</u>	<u>\$24,986</u>	<u>\$ 1,872</u>	<u>\$33,310</u>
Earnings per common share:					
Continuing operations	\$ 0.10	\$ 0.06	\$ 0.29	\$ 0.25	\$ 0.68
Discontinued operations	0.29	0.30	2.85		3.40
	<u>\$ 0.39</u>	<u>\$ 0.36</u>	<u>\$ 3.14</u>	<u>\$ 0.25</u>	<u>\$ 4.08</u>
<b>1987/88</b> (Thousands of dollars except earnings per share data)					
Sales	\$16,524	\$15,994	\$16,126	\$17,175	\$65,819
Gross margin	5,854	4,981	4,977	5,027	20,839
Income from continuing operations	2,121	1,450	1,758	1,650	6,979
Income from discontinued operations	643	185	505	1,233	2,566
Net income	<u>\$ 2,764</u>	<u>\$ 1,635</u>	<u>\$ 2,263</u>	<u>\$ 2,883</u>	<u>\$ 9,545</u>
Earnings per common share:					
Continuing operations	\$ 0.25	\$ 0.17	\$ 0.21	\$ 0.18	\$ 0.81
Discontinued operations	0.07	0.02	0.06	0.15	0.30
	<u>\$ 0.32</u>	<u>\$ 0.19</u>	<u>\$ 0.27</u>	<u>\$ 0.33</u>	<u>\$ 1.11</u>

Quarterly per share data will not necessarily sum to the annual amounts due to changes in weighted average shares outstanding during the periods.



## REPORT OF ERNST & YOUNG INDEPENDENT AUDITORS

Board of Directors and Shareholders  
PENWEST, Ltd.

We have audited the accompanying consolidated balance sheets of PENWEST, Ltd., as of August 31, 1990 and 1989, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the three years in the period ended August 31, 1990. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of PENWEST, Ltd., at August 31, 1990 and 1989, and the consolidated results of its operations and its cash flows for each of the three years in the period ended August 31, 1990, in conformity with generally accepted accounting principles.

Seattle, Washington  
October 12, 1990

*Ernst & Young*



**Board of Directors****Richard E. Engebrecht**

Chairman, President and Chief Executive Officer  
Momentum Distribution, Inc.

**Russell E. Hamachek**

Retired Vice President  
Univar Corporation and Retired President/Chief Executive Officer  
Great Western Malting Co.

**Tod R. Hamachek**

President and Chief Executive Officer  
PENWEST

**David R. Hinson**

Chairman and Chief Executive Officer  
Midway Airlines

**C. Calvert Knudsen**

Vice Chairman  
MacMillan Bloedel, Ltd.

**Curtis P. Lindley**

Retired Chief Executive Officer  
PENWEST

**Harry Mullikin**

Chairman Emeritus  
Westin Hotels and Resorts

**N. Stewart Rogers**

Chairman of the Board  
PENWEST  
Senior Vice President  
Univar Corporation

**William K. Street**

President and Chief Executive Officer  
The Ostrom Company

**James H. Wiborg**

Chairman  
Univar Corporation

**F. Lowry Wyatt**

Consultant and Retired Senior Vice President  
Weyerhaeuser Company

**Officers and Management****Tod R. Hamachek**

President and Chief Executive Officer

**H. Thomas Reed**

President and General Manager  
Penford Products Co.

**Robert E. Miller**

Vice President  
Finance and Chief Financial Officer

**Franklin E. Olsen, Jr.**

Vice President  
Employee Relations and Corporate Secretary

**Robert G. Widmaier**

Vice President  
Technical Director and Chief Innovation Officer

**Jeffrey T. Cook**

Treasurer

**Bradley A. Wiens**

Controller

**Committees,****Headquarters and General Information****Executive****Committee**

James H. Wiborg,  
Chairman

Tod R. Hamachek  
C. Calvert Knudsen  
Curtis P. Lindley  
N. Stewart Rogers

**Audit Committee**

Richard E. Engebrecht,  
Chairman  
Russell E. Hamachek  
William K. Street

**Compensation and Benefits Committee**

F. Lowry Wyatt,  
Chairman  
C. Calvert Knudsen  
N. Stewart Rogers  
James H. Wiborg

**Nominating Committee**

F. Lowry Wyatt,  
Chairman  
William K. Street  
James H. Wiborg

**PENWEST**

Corporate Headquarters  
777-108th Avenue  
N.E., Suite 2390  
Bellevue, WA 98004  
(206) 462-6000

**Penford Products Co.**

Division Headquarters  
1001 First Street, S.W.  
Cedar Rapids, IA 52404

1088 West Sunnyside Rd.  
Idaho Falls, ID 83402

216 First Street  
Richland, WA 99352

**Pacific****Cogeneration, Inc.**

777- 108th Avenue  
N.E., Suite 2390  
Bellevue, WA 98004

**Annual Meeting**

10:30 a.m., Tuesday  
February 12, 1991  
12th Floor Auditorium  
Security Pacific Tower  
Fifth Avenue and University Street  
Seattle, WA

**Form 10-K**

The company files an annual report with the Securities and Exchange Commission on Form 10-K, pursuant to the Securities and Ex-

change Act of 1934. Shareholders may obtain a copy of this report without charge by written request to our headquarters address.

**Legal Counsel**

Preston, Thorgrimson, Shidler, Gates & Ellis  
5400 Columbia Tower  
701 Fifth Avenue  
Seattle, WA 98104

**Auditors**

Ernst & Young  
999 Third Avenue  
Suite 3300  
Seattle, WA 98104

**Investor Relations Counsel**

Corporate Communications, Inc.  
2125 Fifth Avenue  
Seattle, WA 98121  
(206) 728-1778

**Stock Price Data**

Traded National Over-The-Counter  
NASDAQ Symbol: PENW

	Market Price	
	High	Low
<b>1987/88</b>		
Quarter Ended Nov. 30	16.83	8.33
Quarter Ended Feb. 29	13.67	8.83
Quarter Ended May 31	14.17	9.17
Quarter Ended Aug. 31	13.50	9.33
<b>1988/89</b>		
Quarter Ended Nov. 30	13.83	11.67
Quarter Ended Feb. 28	14.75	11.83
Quarter Ended May 31	17.00	13.92
Quarter Ended Aug. 31	16.42	15.50
<b>1989/90</b>		
Quarter Ended Nov. 30	17.00	15.83
Quarter Ended Feb. 28	22.50	16.67
Quarter Ended May 31	30.25	22.00
Quarter Ended Aug. 31	35.13	22.50

The number of common shareholders of record as of November 14, 1990, was 1,860. See Note C to Consolidated Financial Statements for information regarding restrictions on dividends.

Kekst and Co., Incorporated  
437 Madison Ave.  
New York, NY 10022  
(212) 593-2655

**Transfer Agent and Registrar**

First Interstate Bank of California  
Corporate Trust  
P.O. Box 54261  
Los Angeles, CA 90054

**Shareholder Information**

First Interstate Bank, Ltd.  
Shareholder Services  
(800) 522-6645





777-108th Avenue NE  
Suite 2390  
Bellevue, WA 98004