

Annual Report 1984

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# PENWEST LTD.

A new, independent,  
publicly-held company  
with a history of value  
and growth.



PENWEST, LTD. is a major U.S.

agricultural processing company whose principal raw materials are corn and malting barley. PENWEST was formed as a new corporate entity in March, 1984 when it was spun off by Univar Corporation, a Seattle-based company. Its manufacturing businesses are Penick & Ford, Limited and Great Western Malting Co.

Penick & Ford, Limited of Cedar Rapids, Iowa, is a leading producer of treated corn and potato starches for the textile and paper industries. The Company also produces solid corn sweeteners used in pharmaceutical and food products. In addition to its Cedar Rapids facility, Penick & Ford has a potato starch plant in Idaho Falls, Idaho.

Great Western Malting Co. of Vancouver, Washington, is the premier producer of high-quality brewer's malt in the western United States, and also supplies malt to a number of brewers in the Pacific Rim. Great Western's malting operations are located in Vancouver, Washington, Pocatello, Idaho and Los Angeles, California.

PENWEST's corporate headquarters are at 300 One Bellevue Center, 411-108th Ave. N.E., Bellevue, Washington 98004.





Curtis P. Lindley was elected chairman of the board of directors and chief executive officer on March 1, 1984. Before assuming his current post, Mr. Lindley was executive vice president-manufactured products division at Univar Corporation. During his 32-year career at Univar (and companies which later became Univar) he served in a number of executive positions in production, engineering and manufacturing. He earned his engineering degree at Stanford University.

Tod R. Hamachek is president and chief operating officer. He had been senior vice president of Univar's manufacturing group, president and chief executive officer of Great Western Malting Co., and vice president of sales at Great Western. Mr. Hamachek also has executive experience in the paper and printing industries. He earned his BA at Williams College in Williamstown, Massachusetts and his MBA from Harvard Business School.

Franklin E. Olsen is vice president-employee relations, with responsibility for personnel and labor relations. He was director of personnel at Univar and has held similar positions with other Northwest companies. Mr. Olsen was graduated from the University of Puget Sound with majors in business and economics.

Dale C. Leman is vice president-finance and treasurer, and is PENWEST's chief financial officer. He served in a similar capacity at the Physio-Control Corporation of Redmond, Washington, and became a certified public accountant with the international accounting firm of Deloitte, Haskins & Sells. Mr. Leman was graduated from the University of Washington with majors in accounting and business, government and society.

To the Shareholders:

This report is for PENWEST's first fiscal period ending August 31, 1984. The Company has operated independently since March 1, 1984. Prior to becoming independent, PENWEST operations were a part of Univar Corporation.

Earnings for the six-month period ending August 31 were \$1,056,000, compared with \$897,000 in the corresponding period of fiscal 1983, for a gain of 17.7 percent. Revenue was \$75,382,000, up 10.7 percent from \$68,105,000 in 1983. These increases are in line with our internal projections.

The Company's Penick & Ford operations are in an excellent position to benefit from the continued growth in the markets for industrial corn starch products. The paper and textile industries—Penick & Ford's major customers—have shown substantial improvement over 1983, creating a growing demand for the specialty starch products which comprise the division's core products.

PENWEST's Great Western Malting Co. is the leading producer of brewer's malt in the western states. While beer sales nationally have been essentially flat for four years, Great Western serves expanding western markets—including California, the nation's single largest market—and is a major supplier of malt to several of the world's leading brewers, including companies around the Pacific Rim.

PENWEST's selection of an August 31 fiscal year, keyed to agricultural cycles, has resulted in a balance sheet that is much more representative of the Company's actual financial position. Short-term borrowings and inventories at year-end are down sharply.

Other benefits of the spin-off include management of employee compensation and benefit plans more attuned to the agricultural processing industry, streamlined management information systems, and improved management of cash flow.

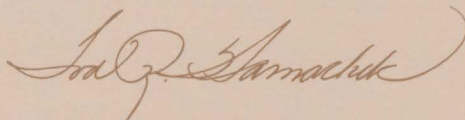
PENWEST is committed to long-term goals and growth, as reflected in the Company's mission statement:

*The Company's purpose is to create the maximum continuing rate of value growth through long-term profit on invested capital and the growth of that capital.*

We believe the Company is well positioned to serve that mission.



Curtis P. Lindley  
Chairman, Chief Executive Officer



Tod R. Hamachek  
President, Chief Operating Officer



# Penick & Ford Limited

Penick & Ford continues to grow as a leading producer of specialty starch products for the paper, textile and solid-based sweetener industries.

The subsidiary's major products have increased in unit sales as well as in share of market. We expect these trends to continue, and anticipate additional growth from new products.

Penick & Ford's principal customers are the major paper manufacturers in the United States. The subsidiary supplies highly modified corn starches for paper coatings as well as starch-based bonding agents for adding tensile strength to paper.

The paper and textile industries are showing strong recovery from the recent recession, and have excellent prospects for long-term growth.

Among the several positive sales trends in the paper industry has been an increasing demand for cationic starches which extend the effective life of high-grade papers. Library of Congress standards, for example, now call for paper with an effective life of 400 years. Penick & Ford is among the leading producers of cationic starches and has recognized expertise as a manufacturer of other specialty starch products.

Penick & Ford invested \$32 million in a major plant expansion and modernization program which was completed in 1981. The result has been significant gains in productivity and capacity at a time of rapidly rising industry demand. Since completion of that project, on-going productivity improvements at the facility continue to enhance profitability.

Penick & Ford showed a strong profit in fiscal 1984, and offers additional opportunities for growth in the years ahead.

Penick & Ford is a major manufacturer of corn starch products for the paper and textile industries. The photo pages in this report are treated with a Penick & Ford product.









Despite a generally soft domestic market for brewer's malt, Great Western recorded both growth and profit in 1984.

In addition to serving a number of growing markets in the West, the division has opened new eastern U.S. markets. A new malt production facility in Pocatello, Idaho, which came on line in late 1981, is the centerpiece of that strategy. Located in the heart of the nation's largest 2-row barley growing areas, the Pocatello facility is an efficient plant with ready access to rail transportation to both eastern and western markets.

Great Western buys barley from farmers in five major growing areas of the West, thus spreading the risk of crop failure over the widest possible geographical area. The advantage of this strategy was underscored recently when an extended drought in Montana caused a poor 1984 harvest. Fortunately, barley from other western areas was plentiful, and an adequate supply of quality western malting barley will be available for Great Western's 1985 sales year.

New markets in the Pacific Rim are served by Great Western's malt house in Vancouver, Washington. Its location in the Port of Vancouver and its efficiency of operation make it highly suitable for serving markets in the Far East.

Great Western has identified a number of key growth strategies for remaining profitable in the future.

It will continue to market malt products in the Company's traditional western markets, while moving aggressively to open new markets in the eastern U.S. and in selected nations of the Pacific Rim.

Stringent cost containment programs already in place are being intensified. Transportation and energy are major cost factors, and Great Western expects to realize further savings by negotiating more favorable transportation contracts and by using energy more efficiently. An example of the latter is the cogeneration facility in Vancouver which produces enough thermal energy to serve the plant while selling surplus electrical power to a public utility district.

Great Western is actively engaged in developing new varieties of malting barley with the expectation that new varieties will offer better malting and/or

Great Western Malting is the West's leading producer of malt for breweries throughout the U.S. and in selected countries of the Pacific Rim.

brewing characteristics or improved agronomic properties. At all times, Great Western's first priority is to continually strive to improve its product quality. This pursuit of quality products and service has distinguished Great Western as one of the world's leading producers of premium brewing malts.

# Great Western Malting Co.



# Financial Review

In reviewing and comparing the financial statements in this report, a detailed understanding of their inherent limitations is necessary. Prior to February 29, 1984, the PENWEST group was operated as the manufacturing subsidiaries of Univar Corporation. During this time, the manufacturing subsidiaries underwent a major physical plant expansion program and were heavily impacted by the recession. Therefore, making comparisons between those periods and the six-month fiscal period ended August 31, 1984 is difficult at best. It was only during recent periods that the businesses began to operate under more consistent conditions.

The most significant event to be considered in any comparison between periods is the physical plant expansion program undertaken at both Penick & Ford and Great Western Malting. By the end of February 1983, \$83 million of plant modernization and expansion additions had been completed over a three-year period.

The second significant event impacting a comparison between periods was the condition of PENWEST's principal markets, the paper industry and malt beverage industry. Penick & Ford's corn wet milling capital improvements came on line during fiscal year 1982 at the depth of the recession. In addition, Penick & Ford needed to expand its sales to better utilize the rebuilt production capacity. Great Western Malting's new Idaho malt plant began production several months prior to completion of the brewing facilities it was intended to supply. And, although demand for malt previously was strong, the brewing market began to weaken and has continued to weaken through the most current fiscal period.

The fiscal year ending February 29, 1984, is the first full year of the periods presented which does not have the disruptive impact of large net plant additions.

Due to the foregoing factors, comparisons of the financial data for those fiscal years when PENWEST operated as part of Univar, with the most recent financial information, must be done carefully. One should focus on the most recent financial periods and on the effect the extensive plant expansion and modernization of the past few years will have on future operations and earnings.

## **Fiscal Year Ended February 28, 1982**

Both the corn wet mill at Cedar Rapids and the malt house at Pocatello were completed in September 1981. Beginning with that month, interest on debt used to finance these facilities was charged to operations. A substantial increase in depreciation during the last half of the year (reflecting the presence of the completed plants) brought depreciation to \$4,510,000 while deferred taxes, reflecting the difference between the straight-line depreciation method used for financial statement purposes and the accelerated basis used for tax, increased significantly. Investment tax credit generated from capital improvements resulted in a net tax refund (benefit) for the period.

Upon completion, both plants immediately faced industry-wide economic challenges. The corn wet milling plant came on-line during a period of weak demand resulting from the 1981/1982 recession's impact on the paper industry. The malting plant operated at low rates until the spring of 1982, when increased demand provided gradually increasing rates of operation.

The second half of this fiscal year was a disappointment. A combination of full interest and depreciation loads, added to weak or delayed market demand, meant that it was not possible to operate the new facilities profitably in the early months of the start-up period.

## **Fiscal Year Ended February 28, 1983**

Operations had a pre-tax loss of \$3,135,000 arising primarily from underutilization of the new plants, reduced margins available in poor markets and from the heavy depreciation and interest charges related to the companies' new manufacturing capacity. At Cedar Rapids, the corn wet mill operated at less than full capacity for the year, and at too low a rate to allow profitability. However, during this year, Penick & Ford implemented an aggressive marketing and sales program, the success of which would be felt in the following periods.



On the West Coast, Great Western Malting customers completed the additional brewing facilities in Southern California, but these plants came on line slowly. For the year, Great Western Malting plants operated at less than desired capacity. Severe price competition also set in, a result of the Staggers Rail Deregulation Act. This Act lowered westbound freight rates significantly, enabling midwestern maltsters to more effectively compete in the West Coast region.

Late in the year, Great Western Malting completed a new cogeneration plant adjacent to the Vancouver, Washington malt house. This facility, financed by stand-alone debt, was designed to reduce and stabilize the cost of heat used in the malting process. The project accounted for most of the net plant additions of \$12,807,000 during the year.

Reflecting the capital expenditures of recent years, depreciation again increased this year to \$6,870,000. Simultaneously, tax deferrals for the year provided an additional cash flow of \$6,051,000. Interest expense charges to operations increased to \$10,533,000, primarily the result of extremely high interest costs on money borrowed on a floating rate basis to finance much of the past three years' plant expansion.

Earnings also were adversely affected by heavy legal fees related to an antitrust suit in the corn wet milling industry. Settlement costs of \$775,000 also were charged to the year's operating results.

#### **Fiscal Year Ended February 29, 1984**

Pretax income for the year totaled \$3,433,000. By March 1983, volume at Penick & Ford had grown to the break-even point, and the Penick & Ford, Limited operations began to consistently report earnings.

Great Western Malting, however, continued to face low demand for malt from its West Coast brewing customers. As a result of excess U.S. malt capacity and flat beer sales, profitability generally weakened. In response to low demand, Great Western Malting temporarily closed its least efficient plant (Los Angeles) in August.

Interest expense dropped over \$2 million from the preceding period, as costs of floating rate debt declined.

#### **Six Months Ended August 31, 1984**

Consolidated sales for the six months ended August 31, 1984 increased 11 percent to \$75,382,000 from \$68,105,000 for the six-month period ended August 31, 1983. Penick & Ford marketing and sales strategies began to pay off. Sales of Penick & Ford's specialty starch products remained strong throughout the current period, reflecting both the new strategies and continued strength of the paper, paperboard and corrugating industries. Domestic malt operations continued to be adversely affected by excess malting capacity, low or no growth in beer sales, and the ongoing shift to light beers. The domestic malt challenges were partially offset by additional Pacific Rim export sales, enabling malt operations to more fully utilize plant capacity. However, continued strength of the U.S. dollar may affect the Company's ability to maintain this export business.

Gross margin increased 13 percent over the comparable six-month period in the preceding year. The improvement reflected efficiencies of higher production levels, primarily in corn products.

For the six months ended August 31, 1984, interest expense amounted to \$4,760,000, up \$426,000 from the preceding comparable period. The increase relates to debt incurred to finance a \$17,000,000 dividend paid to Univar at date of spin-off (See Note 1 on page 10).

#### **Liquidity and Capital Resources**

PENWEST has major variations in grain inventory levels during the year, particularly related to its malt operations. Most barley purchases are made in the fall following harvest. As a result, inventories and related debt financing increase dramatically in the fall with peaks in January and low points in August. Financing of these inventory level changes is provided under bank lines of credit totalling \$44,000,000. Borrowing reached a maximum of \$31,000,000 during the six months ended August 31, and declined to \$13,000,000 at August 31, 1984.

During the last 18 months, capital expenditures have been at essentially a replacement level. Depreciation expense totalled \$3,896,000 and net deferred taxes \$954,000 during the short period ending August 1984. A significant portion of outstanding debt is on a floating rate basis and represents a risk if rates increase. However, fixed-rate mortgage markets, which might be used to permanently finance the past three years' expansion program, have not been attractive. Based on future cash flow from depreciation and deferred taxes, PENWEST should be able to comfortably service existing debt even if earnings do not develop as anticipated. Accordingly, management believes liquidity to be adequate, recognizing that capital expenditures should be relatively low over the next few years.

# Consolidated Balance Sheets (Note 1)

Assets (Thousands of dollars)	August 31, 1984	February 29, 1984	February 28, 1983
<b>Current assets:</b>			
Cash	\$ 204	\$ 1,347	\$ 313
Receivables (Note 4)—			
Trade accounts	16,013	12,924	12,924
Income tax receivable	118	3,607	8,634
Inventories (Notes 3 & 4)	24,974	36,754	40,805
Prepaid expenses and other	965	489	1,630
<b>Total current assets</b>	<b>42,274</b>	<b>55,121</b>	<b>64,306</b>
<b>Property, plant and equipment, at cost (Notes 2 &amp; 4):</b>			
Land	1,061	1,061	1,061
Plant & equipment	122,257	122,054	120,416
Less accumulated depreciation	(37,171)	(33,246)	(25,259)
<b>Net property, plant and equipment</b>	<b>86,147</b>	<b>89,869</b>	<b>96,218</b>
<b>Other Assets</b>	<b>936</b>	<b>560</b>	<b>763</b>
<b>Total</b>	<b>\$129,357</b>	<b>\$145,550</b>	<b>\$161,287</b>
<b>Liabilities and shareholders' equity</b>			
<b>Current liabilities:</b>			
Notes payable (Note 4)		\$ 15,553	\$ 1,000
Current portion of long-term debt	\$ 4,045	3,960	1,539
Accounts payable	7,416	6,207	5,287
Accrued liabilities	4,240	4,034	4,898
Advances from Univar (Note 1)			12,770
<b>Total current liabilities</b>	<b>15,701</b>	<b>29,754</b>	<b>25,494</b>
<b>Revolving credit agreement (Note 4)</b>	<b>13,000</b>	<b>15,000</b>	<b>35,000</b>
<b>Long-term debt (Note 4)</b>	<b>52,381</b>	<b>54,425</b>	<b>54,161</b>
<b>Subordinated debt (Notes 1 &amp; 4)</b>	<b>10,000</b>	<b>10,000</b>	
<b>Deferred items:</b>			
Deferred taxes on income (Note 7)	18,468	17,514	12,258
Deferred credits	1,294	1,400	2,229
<b>Total deferred items</b>	<b>19,762</b>	<b>18,914</b>	<b>14,487</b>
<b>Shareholders' equity (Notes 2, 4 &amp; 5):</b>			
Common stock, par value \$1.00 per share			
Authorized—9,000,000 shares			
Outstanding—2,769,520 shares	2,770	5,058	5,058
Additional paid-in capital	11,689	9,401	8,921
Retained earnings	4,054	2,998	18,166
<b>Total shareholders' equity</b>	<b>18,513</b>	<b>17,457</b>	<b>32,145</b>
<b>Total</b>	<b>\$129,357</b>	<b>\$145,550</b>	<b>\$161,287</b>

The accompanying notes are an integral part of these statements.



Consolidated Statements of Operations (Note 1)

(Thousands of dollars)	Six Months Ended August 31		Year Ended February 29/28		
	1984	1983	1984	1983	1982
		(Unaudited)			
Sales	\$ 75,382	\$ 68,105	\$131,689	\$127,701	\$126,664
Cost of sales	64,452	58,421	112,655	113,520	107,670
Gross margin	10,930	9,684	19,034	14,181	18,994
Operating expenses	4,102	3,591	7,488	6,783	7,719
Income from operations	6,828	6,093	11,546	7,398	11,275
Interest expense	4,760	4,334	8,113	10,533	7,871
Income (loss) before taxes	2,068	1,759	3,433	(3,135)	3,404
Income taxes (benefit) (Notes 2 & 7)	1,012	862	1,601	(2,866)	(3,944)
Net income (loss)	\$ 1,056	\$ 897	\$ 1,832	\$ (269)	\$ 7,348
Earnings per common share and common share equivalent (Note 2):					
Primary	\$0.36				
Fully diluted	\$0.35				

The accompanying notes are an integral part of these statements.

Consolidated Statements of Changes in Financial Position (Note 1)

	Six Months Ended August 31		Year Ended February 29/28		
(Thousands of dollars)	1984	1983	1984	1983	1982
<b>Source of funds:</b>	(Unaudited)				
Operations—					
Net income (loss)	\$ 1,056	\$ 897	\$ 1,832	\$ (269)	\$ 7,348
Depreciation	3,896	3,957	8,021	6,870	4,510
Amortization of other assets	87	102	213	212	232
Deferred income taxes	954	2,587	5,173	6,051	5,630
	5,993	7,543	15,239	12,864	17,720
Contribution from Univar Corporation		243	480	440	4,256
Subordinated note from Univar			10,000		
Long-term debt incurred				19,924	23,522
	5,993	7,786	25,719	33,228	45,498
<b>Application of funds:</b>					
Net plant additions	174	631	1,672	12,807	35,877
Reduction in long-term debt	4,044	19,948	19,736	11,226	838
Dividend to Univar			17,000		
Other	569	256	756	722	118
	4,787	20,835	39,164	24,755	36,833
<b>Working capital:</b>					
Increase (decrease)	1,206	(13,049)	(13,445)	8,473	8,665
Add—beginning working capital	25,367	38,812	38,812	30,339	21,674
Ending working capital	\$ 26,573	\$ 25,763	\$ 25,367	\$ 38,812	\$ 30,339
<b>Increase (decrease) in components of working capital:</b>					
Current assets—					
Cash	\$ (1,143)	\$ 1,899	\$ 1,034	\$ (3,393)	\$ 3,269
Receivables	(400)	(7,386)	(5,027)	(1,607)	11,598
Inventories	(11,780)	(14,923)	(4,051)	3,072	2,378
Prepaid expenses and other	476	(1,171)	(1,141)	406	289
	(12,847)	(21,581)	(9,185)	(1,522)	17,534
Current liabilities—					
Notes payable	(15,553)	4,000	14,553	1,000	
Current portion of long-term debt	85	1,852	2,421	130	289
Accounts payable	1,209	(1,125)	920	(2,815)	(1,706)
Accrued liabilities	206	(859)	(864)	449	789
Advances from Univar		(12,400)	(12,770)	(8,759)	9,497
	(14,053)	(8,532)	4,260	(9,995)	8,869
Increase (decrease)	\$ 1,206	\$ (13,049)	\$ (13,445)	\$ 8,473	\$ 8,665

The accompanying notes are an integral part of these statements.



Consolidated Statements of Shareholders' Equity (Note 1)

(Thousands of dollars)	Common Stock	Additional Paid-in Capital	Retained Earnings	Total Shareholders' Equity
Balance, February 28, 1981	\$ 5,053	\$ 4,230	\$11,087	\$20,370
Net income			7,348	7,348
Contribution from Univar Corporation:				
Idaho Malting Company		3,706		3,706
Pacific Cogeneration	5			5
Executive office expense		545		545
Balance, February 28, 1982	5,058	8,481	18,435	31,974
Net loss			(269)	(269)
Contribution from Univar Corporation:				
Executive office expense		440		440
Balance, February 28, 1983	5,058	8,921	18,166	32,145
Net income			1,832	1,832
Cash dividend distributed to Univar			(17,000)	(17,000)
Contribution from Univar Corporation:				
Executive office expense		480		480
Balance, February 29, 1984	5,058	9,401	2,998	17,457
Net income			1,056	1,056
Retirement of manufacturing subsidiaries' common stock	(5,058)	5,058		
Issuance of PENWEST common stock	2,770	(2,770)		
Balance, August 31, 1984	\$ 2,770	\$11,689	\$ 4,054	\$18,513

The accompanying notes are an integral part of these statements.

## Notes to Consolidated Financial Statements

(Information as of August 31, 1983, and for the six-month period then ended is unaudited)

### Note 1: Organization and Transactions with Univar Corporation

PENWEST, LTD. was incorporated as a subsidiary of Univar Corporation on September 20, 1983. On February 29, 1984, Univar transferred to PENWEST all of the outstanding stock of its manufacturing subsidiaries including Penick & Ford, Limited, Idaho Malting Company, Pacific Cogeneration, Inc. and Great Western Malting Export Corporation. On March 1, 1984, Univar spun off PENWEST to its shareholders by distributing one share of PENWEST stock for each two shares of Univar stock owned as of February 29, 1984.

The consolidated financial statements for the six months ended August 31, 1984 include PENWEST and its wholly-owned subsidiaries. The combined financial statements for the six months ended August 31, 1983 and the fiscal years ended February 29/28, 1984, 1983 and 1982 include the accounts of the manufacturing subsidiaries of Univar. All intercompany balances and transactions have been eliminated. The financial statements for the six months ended August 31, 1983 have not been audited. In the opinion of management, all adjustments necessary for a fair presentation of the results of this period have been included. All such interim adjustments are of a normal, recurring nature.

The combined financial statements of the manufacturing subsidiaries of Univar include an estimate of corporate office expense which management has estimated would have been incurred by the manufacturing subsidiaries operating independently. The after-tax impact on earnings of this allocation was recorded as a contribution to additional paid-in capital of the manufacturing subsidiaries.

The manufacturing subsidiaries also borrowed under temporary advances from Univar. Interest on these advances was charged based on Univar's short-term borrowing rate. This resulted in interest costs of \$68,000 (an effective annual rate of 13 percent) for the six months ended August 31, 1983 and \$212,000, \$2,518,000, and \$3,041,000 (effective annual rates of 10 percent, 13 percent and 17 percent) for fiscal years February 29/28, 1984, 1983 and 1982, respectively.

On February 29, 1984, Penick & Ford, Limited distributed a cash dividend of \$17,000,000 to Univar. Simultaneously, Univar loaned \$10,000,000 to Penick & Ford, Limited on a subordinated note for five years at an interest rate of 13 percent (See Note 4). Since these transactions occurred at the spin-off date, the related interest expense is not reflected in the combined financial statements for the periods prior to the six months ended August 31, 1984.

Univar continues to guarantee certain debts of PENWEST. In consideration thereof, PENWEST granted Univar a warrant to purchase shares that together with the then outstanding common stock would equal 20 percent of PENWEST common stock. The per-share exercise price of the warrant is \$6.40. The price was based on the average trading price for 10 days subsequent to the distribution record date. The warrant, which expires in September 1993, is transferable and is subject to certain anti-dilution provisions. Univar has also agreed to certain restrictions on the exercise and holding period of shares acquired under the warrant.

In connection with the spin-off, PENWEST entered into a management services agreement with Univar to provide an orderly separation of the two businesses. The agreement makes available to PENWEST (for a three-year period) certain services from Univar including financial, tax and accounting, and personnel services as needed. In addition, each company has agreed to make records and personnel available to the other in connection with the preparation of tax returns, tax audits, claims and litigation.

### Note 2: Summary of Significant Accounting Policies

#### 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 in computing depreciation for financial reporting purposes. For income tax purposes, the Company generally uses accelerated methods.

Interest has been capitalized on major construction projects while in progress. Interest of \$947,000 and \$3,880,000 for fiscal years ended February 28, 1983 and 1982 was capitalized. No interest was capitalized in the six months ended August 31, 1984, or in the fiscal year ended February 29, 1984.

#### Income Taxes

Income taxes are provided regardless of the period when such items will be deductible for tax purposes. Investment tax credits are recognized as a tax reduction in the year in which they can be utilized.



### Earnings Per Share

Earnings per common share and common share equivalents were computed by dividing net income by the weighted average number of shares of common stock and common share equivalents outstanding during the period (2,983,996 for primary and 3,036,401 for fully diluted). Stock options and warrants to purchase stock are considered to be common share equivalents when dilutive, using the treasury stock method. (Under this method, \$28,000 of assumed after-tax interest savings was added to net income for the computation of primary earnings per share.) Since the Company began independent operations on March 1, 1984, earnings per share information has not been presented for prior periods.

### Segment Information—Major Customers

PENWEST operates principally in one line of business—agricultural processing. Two major customers accounted for sales of \$28,481,000 and \$7,377,000 in the six months ended August 31, 1984; \$29,345,000 and \$6,642,000 in the six months ended August 31, 1983; \$53,675,000 and \$12,120,000 in the fiscal year ended February 29, 1984; \$59,223,000 and \$12,739,000 in the fiscal year ended February 28, 1983; and \$47,613,000 and \$16,488,000 in the fiscal year ended February 28, 1982.

### Preferred Stock

PENWEST has 1,000,000 shares of preferred stock, \$1.00 par value, authorized of which none are issued or outstanding.

### Note 3: Inventories

Inventories 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.

Inventories consisted of:

(Thousands of dollars)	August 31, 1984	February 29, 1984	February 28, 1983
Raw materials, supplies and other	\$12,455	\$22,255	\$27,526
Work in progress	1,171	1,525	1,385
Finished goods	11,348	12,974	11,894
Total inventories	\$24,974	\$36,754	\$40,805

### Note 4: Long-Term Debt and Revolving Credit Agreement

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

(Thousands of dollars)	August 31, 1984	February 29, 1984	February 28, 1983
10¾ percent promissory note, payable in installments to 2001, secured by certain real property and equipment	\$20,429	\$20,540	\$20,748
9 percent promissory note, payable in installments to 1998, secured by certain property and equipment	17,144	17,445	13,506
8¾ percent mortgages, payable in installments to 1991, secured by certain real property and equipment	11,044	11,532	12,446
Term loan, with variable interest keyed to certificate of deposit rates plus 2.1 percent, payable in installments to 1988, secured by certain real property and equipment	7,809	8,868	9,000
13 percent unsecured subordinated promissory note, payable February 29, 1989 to Univar Corporation, with annual interest-only payments due March 1 of each year	10,000	10,000	
	66,426	68,385	55,700
Less—current portion	4,045	3,960	1,539
Net long-term debt	\$62,381	\$64,425	\$54,161

The 8¾ percent mortgages are guaranteed by Univar Corporation. The 10¾ percent and 9 percent promissory notes carry a combined maximum guarantee by Univar of \$20,000,000.

Maturities of long-term debt for the fiscal years ending August 31, 1985 through 1989 are as follows (Thousands of dollars):

1985	\$ 4,045
1986	\$ 4,228
1987	\$ 4,428
1988	\$ 3,986
1989	\$12,772

Through a revolving credit agreement with four banks, the Company and its subsidiaries may borrow up to \$44,000,000 at prime rate plus 1.5 percent, or certificate of deposit rate plus 2.3 percent, or Bankers' Acceptance rate plus fees and expenses. The approximate average aggregate borrowing and weighted average interest rates were \$23,500,000 and 14.2 percent in the six months ended August 31, 1984. The maximum amount of borrowings during the six month period was \$31,000,000 on March 1, 1984. The borrowings are secured by inventories and accounts receivable. The revolving credit agreement includes, among other terms, various limitations on long-term indebtedness, minimum net worth balances and working capital ratios, and restrictions on PENWEST's ability to purchase or redeem its own stock or pay cash dividends. Under the most restrictive of these terms, the minimum net worth test, minimum net worth for the period ending August 31, 1984 must be at least \$16,000,000. The term of this agreement is automatically extended 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 90 days after notice of election to withdraw. At February 29, 1984, \$15,553,000 of borrowings were classified as current since it was the Company's intention to repay that amount by August 31, 1984.

#### Note 5: Stock Options and Warrant

As of August 31, 1984, options to purchase 76,000 common shares were outstanding under PENWEST's stock option plan, none of which were exercisable. The option prices, which were equivalent to market price at the date of grant, range from \$6.25 to \$10.13 per share. The plan, which authorizes 125,000 common shares, is subject to shareholder approval.

The Company also has granted a warrant to Univac Corporation to purchase 692,380 shares of common stock (See Note 1).

#### Note 6: Pension Plans

Substantially all employees of PENWEST and its subsidiaries are covered by defined benefit pension plans. Total pension expense amounted to \$276,000 and \$394,000 for the six months ended August 31, 1984 and 1983; and \$788,000, \$1,297,000 and \$899,000 for fiscal years ended February 29/28, 1984, 1983 and 1982, which includes amortization of prior service costs over periods ranging up to 30 years.

It is the policy of PENWEST to fund amounts necessary to meet at least the minimum funding requirements of the Employee Retirement Income Security Act of 1974.

As of January 1, 1984, benefit and asset information for the salaried plan of PENWEST and its subsidiaries and the negotiated hourly plan sponsored by Penick & Ford, Limited was as follows:

(Thousands of dollars)

Actuarial present value of plan benefits as of January 1, 1984:

Vested	\$8,258
Non-vested	148
	\$8,406
Net assets available for benefits	\$6,920

Net assets available for plan benefits include the market value of fund assets (\$4,068,000) and accumulated amounts charged to operations, but not yet funded (\$2,852,000). The actuarial present value of plan benefits was determined using a rate of return of 9 percent.

Certain employees are covered under jointly-sponsored, collectively-bargained plans. Provisions for the multiemployer Pension Plan Amendments Act of 1980 require participating employers to assume a proportionate share of multiemployer plans unfunded vested benefits in the event of withdrawal from or termination of the plan. Provisions of the act may have the effect of requiring increased contributions in future years.



# Note 7: Income Taxes

Income tax expense consisted of the following:

(Thousands of dollars)	August 31,	August 31,	February 29/28		
	1984	1983	1984	1983	1982
		(Unaudited)			
Current					
Federal	\$ 39	\$ (1,785)	\$(3,692)	\$(8,801)	\$(9,847)
State	19	60	120	(116)	273
	58	(1,725)	(3,572)	(8,917)	(9,574)
Deferred					
Federal	877	2,550	5,100	5,976	5,405
State	77	37	73	75	225
	954	2,587	5,173	6,051	5,630
Total provision (benefit)	\$1,012	\$ 862	\$ 1,601	\$(2,866)	\$(3,944)

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

(Thousands of dollars)	August 31,	August 31,	February 29/28		
	1984	1983	1984	1983	1982
		(Unaudited)			
Depreciation	\$2,355	\$2,357	\$4,714	\$5,086	\$3,329
Capitalized interest				446	1,814
Capitalized repairs					201
Capitalized sales tax		28	55	340	100
Plant closing reserve	68	202	404	179	186
Reductions due to net operating loss and tax credit carryforward	(1,469)				
Total deferred provision	\$ 954	\$2,587	\$5,173	\$6,051	\$5,630

An analysis of the difference between the actual tax expense and the expected expense using the Federal statutory rate is set forth below:

(Thousands of dollars)	August 31,	August 31,	February 29/28		
	1984	1983	1984	1983	1982
		(Unaudited)			
Federal tax at statutory rate	\$ 951	\$ 809	\$1,580	\$(1,442)	\$1,566
State taxes, net of Federal tax benefit	52	52	104	(22)	269
Investment tax credit and other—net	9	1	(83)	(1,402)	(5,779)
Total provision (benefit)	\$1,012	\$ 862	\$1,601	\$(2,866)	\$(3,944)

The Company has net operating loss and tax credit carryforwards for income tax purposes of \$2,879,000 and \$61,000 at August 31, 1984. These carryforwards are available to offset future taxable income and taxes payable, respectively, through 1999. Should these be utilized, the deferred tax liability will be increased by \$1,469,000.

Any tax adjustments attributable to the manufacturing subsidiaries of Univar for the periods prior to the spin-off will be borne by PENWEST. The consolidated tax returns of Univar Corporation, which include the manufacturing subsidiaries, have been audited by the Internal Revenue Service and settled through February 28, 1979.

**Note 8: Leases**

Rental expense was approximately \$397,000 and \$395,000 for the six months ended August 31, 1984 and 1983; and \$791,000, \$541,000 and \$351,000 for the fiscal years ended February 29/28, 1984, 1983 and 1982.

Future lease payments as of August 31, 1984 for non-cancellable operating leases having initial lease terms of more than one year, are shown below:

Years ending August 31 (Thousands of dollars)	Operating Leases
1985	\$ 867
1986	841
1987	790
1988	520
1989	372
Thereafter	245
Total minimum payments	\$3,635

Total minimum lease payments for operating leases, as shown above, have not been reduced by minimum sublease rentals of \$1,027,000 due in the future under non-cancellable leases.

**Note 9: Litigation**

PENWEST and its subsidiaries are involved in various legal actions and claims which are considered normal to the Company's business.

A class action suit filed against Penick & Ford, Limited has been settled. The settlement in the federal cases was approved by the district court, but an appeal has been filed by one objector. A similar state case has also been settled with the approval of the court.

In the opinion of management, these claims, when finally concluded, will not have material adverse impact on the consolidated financial position of PENWEST.

**Note 10: Quarterly Financial Data (Unaudited)**

Summarized unaudited quarterly financial data for the six months ended August 31, 1984, and for fiscal years ended February 29/28, 1984, 1983 and 1982 are as follows (see Note 1):

(Thousands of dollars, except earnings per share)	Sales	Gross Margin	Net Income	Primary EPS	Fully Diluted EPS
Six months ended August 31, 1984					
First quarter	\$ 37,619	\$ 5,660	\$ 502	\$ .18	\$ .18
Second quarter	37,763	5,270	554	.18	.17
Total—two quarters	\$ 75,382	\$10,930	\$1,056	\$ .36	\$ .35
1983/1984					
First quarter	\$ 34,103	\$ 4,834	\$ 379		
Second quarter	34,002	4,850	518		
Third quarter	30,860	5,039	775		
Fourth quarter	32,724	4,311	160		
Total	\$131,689	\$19,034	\$1,832		
1982/1983					
First quarter	\$ 36,700	\$ 5,223	\$ 308		
Second quarter	33,448	3,798	(418)		
Third quarter	29,170	2,407	( 91)		
Fourth quarter	28,383	2,753	( 68)		
Total	\$127,701	\$14,181	\$ (269)		
1981/1982					
First quarter	\$ 32,614	\$ 5,891	\$2,499		
Second quarter	33,425	5,312	2,514		
Third quarter	29,083	3,056	984		
Fourth quarter	31,542	4,735	1,351		
Total	\$126,664	\$18,994	\$7,348		

The gross margin amounts include items previously reported as other income and expense.









**Note II: Effects of Inflation (Unaudited)**

In accordance with generally accepted accounting principles, PENWEST financial statements are presented in terms of actual historical costs only. The following supplementary information, required by the Statement of Financial Accounting Standards No. 33, attempts to demonstrate the effects of general inflation (constant dollar method) and the effects of changes in specific prices of certain assets used by the Company (current cost method) on financial statement reporting.

The constant dollar method uses the Consumer Price Index (CPI) to restate historical cost statements into constant dollars of equivalent purchasing power. The current cost method uses price changes of specific assets (inventory and fixed assets) to measure the effects of inflation. Appropriate external cost indices and current construction cost information were used to restate these assets.

Both methods require the use of assumptions and estimates. Neither method considers technological or other improvements that would be made if operating capacity were replaced. In addition, neither method adequately takes into account the differing effects of inflation between different industries. As such, the information provided, in light of its experimental nature, is not a precise indicator of inflationary effects.

**Consolidated Supplemental Inflation-Adjusted Statement of Operations**

For the fiscal six months ended August 31, 1984 (Thousands of dollars)	As Reported in the Primary Statements	General Inflation (Constant Dollar)	Specific Prices (Current Cost)
Net sales	\$75,382	\$75,382	\$75,382
Cost of sales	64,452	66,612	68,725
Other operating expenses—net	4,102	4,103	4,104
Interest expense	4,760	4,760	4,760
	73,314	75,475	77,589
Net income (loss) before taxes	2,068	(93)	(2,207)
Income taxes	1,012	1,012	1,012
Net income (loss)	\$ 1,056	\$ (1,105)	\$ (3,219)
Depreciation and amortization included in cost of goods sold and other operating expenses above	\$ 3,983	\$ 5,143	\$ 6,374
Purchasing power gain from holding net monetary liabilities during the six months		\$ 2,432	\$ 2,432
Increase in specific prices (current cost) of inventories and property, plant and equipment held during the six months			\$ 5,600
Less effect of increase in general price level			2,975
Increase in specific prices over increase in general price level			\$ 2,625

At August 31, 1984, current cost of inventories was \$24,661 and current cost of property, plant and equipment, net of accumulated depreciation was \$164,492.

Five-Year Comparison of Selected Supplemental  
Financial Data Adjusted for Effects of Changing Prices

(In average 1984 fiscal period dollars (except "historical" amounts))

(Thousands of dollars, except per share data)	Six Months Ended	Fiscal Years Ended February 29/28			
	August 31, 1984	1984	1983	1982	1981
Net sales:					
Historical	\$ 75,382	\$131,689	\$127,701	\$126,664	\$108,689
Constant dollar	75,382	135,906	136,857	142,044	133,818
Net income (loss):					
Historical	1,056	1,832	(269)	7,348	3,776
Constant dollar	(1,105)	(3,186)	(4,422)	3,494	(604)
Current cost	(3,219)	(8,758)	(9,876)	(2,204)	(4,638)
Net income (loss) per share:					
Historical	.36				
Constant dollar	(.40)				
Current cost	(1.16)				
Purchasing power gain from holding net monetary liabilities during the year	2,432	4,425	3,893	7,009	8,555
Increase in specific prices of inventories and properties over (under) increase in general price level	2,625	5,754	6,550	15,322	(2,027)
Net assets at year-end:					
Historical	18,513	17,457	32,145	31,974	20,370
Constant dollar	41,595	40,417	55,378	56,956	41,108
Current cost	95,405	102,953	118,424	119,900	92,785
Market price per share at year-end:					
Historical	10.00				
Constant dollar	9.88				
Average consumer price index	309.4	299.8	288.7	275.9	251.3

Auditors' Report

To the Shareholders of PENWEST, LTD.:

We have examined the consolidated balance sheet of PENWEST, LTD. (a Delaware corporation) and subsidiaries as of August 31, 1984 and the related consolidated statements of operations, shareholders' equity and changes in financial position for the six months then ended. We have also examined the combined balance sheets of the Manufacturing Subsidiaries of Univar Corporation (Penick & Ford, Limited; Idaho Malting Company; Pacific Cogeneration, Inc. and Great Western Malting Export Corporation) as of February 29/28, 1984 and 1983, and the related combined statements of operations, shareholders' equity and changes in financial position for each of the three years ended February 29/28, 1984, 1983 and 1982. 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 consolidated and combined financial statements referred to above present fairly the financial position of PENWEST, LTD. as of August 31, 1984 and of the Manufacturing Subsidiaries of Univar Corporation as of February 29/28, 1984 and 1983, and the results of their operations and the changes in their financial position for the six months ended August 31, 1984 and for each of the three years ended February 29/28, 1984, 1983 and 1982, respectively, in conformity with generally accepted accounting principles applied on a consistent basis.

Seattle, Washington  
October 5, 1984

Arthur Andersen & Co.



### Board of Directors

Richard E. Engebrecht  
President and Chief  
Operating Officer,  
Univar Corporation

Russell E. Hamachek  
Chairman of Western  
Acquisitions Group, Inc.  
Retired Vice President,  
Univar Corporation and  
President, Great Western  
Malting Co.

Tod R. Hamachek  
President and Chief  
Operating Officer  
PENWEST, LTD.

C. Calvert Knudsen  
Vice Chairman,  
MacMillan Bloedel Ltd.

Curtis P. Lindley  
Chairman and Chief  
Executive Officer  
PENWEST, LTD.

N. Stewart Rogers  
Senior Vice President-  
Finance  
Univar Corporation

William K. Street  
President,  
The Ostrom Company

James H. Wiborg  
Chairman and Chief  
Executive Officer  
Univar Corporation

Lowry Wyatt  
Consultant and Retired  
Senior Vice President  
Weyerhaeuser Company

### Officers

Curtis P. Lindley  
Chairman  
Chief Executive Officer

Tod R. Hamachek  
President  
Chief Operating Officer

Dale C. Leman  
Vice President-Finance  
Secretary  
Treasurer

Charles M. Widmer  
President of  
Penick & Ford, Limited

Ronald B. Vogel  
Vice President and General  
Manager of Great Western  
Malting Co.

Franklin E. Olsen, Jr.  
Vice President-Employee  
Relations

### Committees

#### Executive Committee

James H. Wiborg  
Tod R. Hamachek  
C. Calvert Knudsen

Curtis P. Lindley  
N. Stewart Rogers

#### Audit/Pension Committee

N. Stewart Rogers  
Richard E. Engebrecht

Russell E. Hamachek  
William K. Street

#### Compensation Committee

Lowry Wyatt  
C. Calvert Knudsen

William K. Street  
James H. Wiborg

## Annual Meeting

2 p.m. Thursday, December 6, 1984

Bellevue Athletic Club

11200 S.E. 6th

Bellevue, WA 98004

Form 10-K.

The Company files an annual report with the Securities and Exchange Commission on Form 10-K, pursuant to the Securities Exchange Act of 1934. Shareholders may obtain a copy of this report without charge by writing:

Dale C. Leman,  
Vice President-Finance  
and Treasurer  
PENWEST, LTD.  
300 One Bellevue Center  
411-108th Ave. N.E.  
Bellevue, WA 98004

Transfer Agent and Registrar  
Seattle-First National Bank  
Stock Transfer Services  
Box 24186  
Seattle, Washington 98124

Legal Counsel  
Shidler, McBroom & Gates  
3500 First Interstate  
Seattle, Washington 98104

Auditors  
Arthur Andersen & Co.  
Norton Building  
801 Second Avenue  
Seattle, Washington 98104

Investor Relations Counsel  
Corporate Communications, Inc.  
Suite 412  
200 West Mercer  
Seattle, Washington 98119

Stock Price Data  
Traded: Over-The-Counter  
NASDAQ Symbol: PENW

Common stock of PENWEST, LTD.  
began trading on March 1, 1984. The  
range of high and low Bid-Ask  
quotations from that date through the  
end of the Company's 1984 fiscal year  
August 31 is as follows:

	High		Low	
	Bid	Ask	Bid	Ask
Three months ended August 31, 1984	11 <sup>1</sup> / <sub>4</sub>	12	6 <sup>1</sup> / <sub>4</sub>	7
Three months ended May 31, 1984	7	7 <sup>3</sup> / <sub>4</sub>	5 <sup>1</sup> / <sub>2</sub>	6 <sup>1</sup> / <sub>8</sub>