SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

# FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 1998

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ______ to ______

Commission file number Q4823

ACME UNITED CORPORATION
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| CONNECTICUT | 06-0236700 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

| | |
|---|---|
| 75 KINGS HIGHWAY CUTOFF, FAIRFIELD, CONNECTICUT | 06430 |
| (Address of principal executive offices) | (Zip Code) |

Registrant's telephone number, including area code:
(203) 332-7330

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [ ]

Registrant had 3,377,488 shares outstanding as of November 11, 1998 of its $2.50 par value Common Stock.



ACME UNITED CORPORATION





## PART I. FINANACIAL INFORMATION

ACME UNITED CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS
(UNAUDITED)
(all amounts in thousands)

| | September 30 1998 | December 31 1997 |
|---|---|---|
| ASSETS | | |
| Current Assets: | | |
| Cash and cash equivalents | $ 331 | $ 25 |
| Accounts receivable, net | 11,955 | 7,446 |
| Inventories: | | |
| Finished goods | 5,338 | 7,658 |
| Work in process | 2,118 | 1,229 |
| Raw materials and supplies | 4,885 | 5,194 |
| | 12,341 | 14,081 |
| Prepaid expenses and other current assets | 901 | 176 |
| Total current assets | 25,528 | 21,728 |
| Property, plant and equipment: | | |
| Land | 219 | 205 |
| Buildings | 2,178 | 2,126 |
| Machinery and equipment | 16,343 | 15,528 |
| | 18,740 | 17,859 |
| Less accumulated depreciation | 12,022 | 11,624 |
| | 6,718 | 6,235 |
| Other assets | 825 | 837 |
| Goodwill | 513 | 527 |
| Total assets | $ 33,584 | $ 29,327 |

See notes to condensed consolidated financial statements.



ACME UNITED CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS - continued
(UNAUDITED)
(all amounts in thousands)

| | September 30 1998 | December 31 1997 |
|---|---|---|
| LIABILITIES | | |
| Current Liabilities: | | |
| Cash overdraft | $ 813 | $ 2,538 |
| Accounts payable | 3,863 | 3,525 |
| Current portion of long term debt | 14,542 | 1,189 |
| Restructuring liability | --- | 27 |
| Other accrued liabilities | 4,662 | 3,902 |
| Total current liabilities | 23,880 | 11,181 |
| Long term debt, less current portion | 3,276 | 11,852 |
| Total liabilities | 27,156 | 23,033 |
| STOCKHOLDERS' EQUITY | | |
| Common stock, par value $2.50 : Authorized-4,000,000 shares; Issued-3,482,495 shares in 1998 and 3,473,995 shares in 1997 | 8,706 | 8,685 |
| Additional paid-in capital | 2,251 | 2,238 |
| Retained-earnings deficit | (2,617) | (2,714) |

| | | |
|---|---|---|
| Accumulated other comprehensive loss - translation adjustment | (1,223) | (1,226) |
| Treasury stock-111,620 shares | (689) | (689) |
| Total stockholders' equity | 6,428 | 6,294 |
| Total liabilities and stockholders' equity | $ 33,584 | $ 29,327 |

See notes to condensed consolidated financial statements.



ACME UNITED CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE INCOME
(UNAUDITED)
(all amounts in thousands, except per share amounts)

| | Three Months Ended September 30 | | Nine Months Ended September 30 | |
|---|---|---|---|---|
| | 1998 | 1997 | 1998 | 1997 |
| Revenues: | | | | |
| Net sales | $ 13,382 | $ 12,715 | $ 37,145 | $ 36,449 |
| Other income | 125 | 104 | 257 | 1,046 |
| Total revenues | 13,507 | 12,819 | 37,402 | 37,495 |
| Costs and expenses: | | | | |
| Cost of goods sold | 10,289 | 9,316 | 28,036 | 26,499 |
| Selling, general and administrative expenses | 2,737 | 2,925 | 8,133 | 8,742 |
| Interest expense | 412 | 354 | 1,113 | 960 |
| Restructuring and other charges | 1 | --- | 8 | 530 |
| Total expenses | 13,439 | 12,595 | 37,290 | 36,731 |
| Income before income taxes | 68 | 224 | 112 | 764 |
| Provision for income taxes | (2) | 38 | 15 | 75 |
| Net income | 70 | 186 | 97 | 689 |
| Other comprehensive income (expense) - foreign currency translation | 34 | (29) | 3 | (185) |
| Comprehensive income | $ 104 | $ 157 | $ 100 | $ 504 |
| Basic earnings per share | $ 0.02 | $ 0.06 | $ 0.03 | $ 0.21 |
| Diluted earnings per share | $ 0.02 | $ 0.05 | $ 0.03 | $ 0.19 |
| Weighted average number of common shares outstanding- denominator for basic per share computation | 3,371 | 3,354 | 3,370 | 3,351 |
| Weighted average number of dilutive stock options outstanding | 365 | 317 | 348 | 315 |
| Denominator for diluted per share computation | 3,736 | 3,671 | 3,718 | 3,666 |

See notes to condensed consolidated financial statements.



ACME UNITED CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)
(all amounts in thousands)

| | Nine Months Ended September 30 | |
|---|---|---|
| | 1998 | 1997 |
| Operating activities: | | |
| Net income | $ 97 | $ 689 |
| Adjustments to reconcile net income to net cash used by operating activities: | | |
| Gain on sale of marketing rights | --- | (846) |
| Depreciation | 782 | 772 |
| Amortization | 17 | 81 |
| Increase in deferred income taxes | 56 | 22 |
| Gain on disposal of property, plant, and equipment | (90) | --- |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (5,007) | (3,872) |
| Inventories | 1,720 | (2,481) |
| Prepaid expenses and other current assets | (259) | (158) |
| Other assets | (15) | (10) |
| Accounts payable | 311 | 836 |
| Other accrued liabilities | 780 | 663 |
| Net cash used by operating activities | (1,608) | (4,304) |
| Investing activities: | | |
| Capital expenditures | (1,474) | (1,439) |
| Proceeds from sales of property, plant, and equipment | 446 | 258 |
| Proceeds from sale of marketing rights | --- | 1,915 |
| Net cash (used) provided by investing activities | (1,028) | 734 |
| Financing activities: | | |
| Proceeds from long term debt and credit arrangements | 3,488 | 3,788 |
| Payments on long term debt and credit arrangements | (578) | (705) |
| Stock options exercised | 34 | 139 |
| Net cash provided by financing activities | 2,944 | 3,222 |
| Effect of exchange rate changes on cash | (2) | 3 |
| Net change in cash and cash equivalents | 306 | (345) |
| Cash and cash equivalents at beginning of period | 25 | 427 |
| Cash and cash equivalents at end of period | $ 331 | $ 82 |

See notes to condensed consolidated financial statements.



NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1 -
In the opinion of management, the accompanying condensed consolidated financial statements contain all adjustments necessary to present fairly the financial position, results of operations and cash flows. However, the financial statements do not include all of the disclosures normally required by generally accepted accounting principles or those normally made in the Company's annual report on Form 10-K. Please refer to the Company's annual report on Form 10-K for the year ended December 31, 1997 for such disclosures. The condensed balance sheet as of December 31, 1997 was derived from the audited financial statements as of that date. However, certain reclassifications have been made thereto to conform to the 1998 presentation. The results of operations for the nine months

ended September 30, 1998 are not necessarily indicative of the results to be expected for the full year.

Note 2 -

The Company adopted Financial Accounting Standards Board Statement of Financial Accounting Standards No. 128, "Earnings Per Share" ("SFAS 128") as of its December 31, 1997 year-end. As such, per share amounts for 1997 as presented herein reflect the adoption of SFAS 128.

Note 3 -

As of January 1, 1998, the Company adopted SFAS 130, "Reporting Comprehensive Income". The adoption of this Statement had no impact on the Company's net income or shareholders' equity. Under SFAS 130 the Company's foreign currency translation adjustments, which are reported separately in shareholders' equity, are also required to be included in the determination of other comprehensive income or loss. The prior year financial statements have been reclassified to conform to the requirements of SFAS 130.

Note 4 -

The Company has been involved in certain environmental matters. Additionally, the Company has been involved in numerous legal actions relating to the use of certain latex products, which the Company distributes, but does not manufacture. The Company is one of many defendants. The Company has been released from the majority of the lawsuits. While four lawsuits remain, they are still in preliminary stages and there is no indication the Company's products were involved. Based on information available, the Company believes that it is not reasonably possible that a material adverse impact on financial position, results of operations, or liquidity, may result from environmental and product liabilities, either individually or in aggregate.

The Company's Year 2000 Task Force is completing its assessment of the impact of the Year 2000. The Task Force is in the process of determining an action plan for testing and validating all systems. In the U.S., the Company implemented a new information system in 1997, which it believes addresses any computer system issues related to the Year 2000. Management believes that the Year 2000 issue will not materially affect future financial results.



Note 5 -

Long term debt consisted of the following:
(all amounts in thousands)

| | September 30 1998 | December31 1997 |
|---|---|---|
| Revolving Line of Credit | $ 11,780 | $ 10,915 |
| Revolving Loan | 2,758 | --- |
| Term Loan | 1,385 | 600 |
| Mortgage and Other Notes Payable | 1,895 | 1,526 |
| | 17,818 | 13,041 |
| Less, Current Portion | 14,542 | 1,189 |
| | $ 3,276 | $ 11,852 |

The Company's Revolving Line of Credit and Term Loan are due in May of 1999. The Company is currently in negotiations with its lender to extend the maturity date and fully expects to complete such arrangement prior to December of 1998.

On May 19, 1998, the Company negotiated a $3,500,000 Revolving Loan with its current lender. Under this agreement, the amount available is determined using an asset based formula. The loan matures May 19, 2001 and bears interest at the prime rate.

# MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

For the Three and Nine Months Ended September 30, 1998

## Results of Operations

### Net Sales

Consolidated net sales for the quarter ended September 30, 1998 were $13,382,000 compared with $12,715,000, or 5% higher, for the same period last year. In 1997, Acme sold the marketing rights of certain wound care products to Seton Healthcare International Limited. In 1998, Acme acquired the Rotex Division of Esselte Canada. Excluding the impact of Seton, net sales increased by $1,033,000, or 8%, compared with the third quarter of 1997 with Rotex contributing $367,000, or 36%, of the increase in net sales.

Net sales were $37,145,000 for the first nine months of 1998, compared with net sales of $36,449,000, or 2% higher, for the first nine months of 1997. Net sales in 1997 included $1,973,000 for Seton products. Excluding Seton, net sales increased by $2,669,000, or 8%, compared with the first nine months of 1997 with Rotex contributing $1,285,000, or 48%, of the increase in net sales.

Consumer products net sales in the U.S. of $7,287,000 in the third quarter of 1998 increased 13% compared with $6,463,000 in the third quarter 1997. Sales of Tagit!, the patented children's scissor line, began during the second quarter with shipments to Kmart, Staples, Office Depot and others in time for the back-to-school season. Tagit! accounted for about half of the increase in net sales in the scissor category. Sales growth in the first aid product line resulted from sourcing and repackaging products to leverage distribution channels in combination with increased sales to existing customers and new customers. The company expects to exploit the innovative concept of Tagit! by expanding existing product lines including adult scissors and rulers.

Medical products net sales of $2,730,000 in the third quarter of 1998 decreased $554,000, or 17%, compared with $3,284,000 in the third quarter 1997. Excluding Seton, net sales decreased $188,000, or 6%. The decline resulted from the lack of orders from a single Asian customer with core sales remaining steady. In June, the division won a supply contract with a national alternative care distributor to consolidate minor procedure kits around its product line. Revenues from this contract are expected to exceed $4 million over the next three years with shipments beginning during the quarter.

International sales increased by 13% for the third quarter primarily due to Canada. Excluding currency fluctuations, international sales for the third quarter of 1998 were 18% higher than the third quarter of 1997. Canada sales increased 32% primarily due to the purchase of the Rotex Division of Esselte Canada. Excluding the acquisition, third quarter sales of the ongoing business improved 18% over prior year levels as the acquisition of Rotex has lead to strong growth in the existing Acme product lines. European sales were flat with 1997 levels.

### Gross Profit

Consolidated gross profit for the third quarter of 1998 was $3,093,000 (23.1% of net sales) compared with $3,399,000 (26.7% of net sales) for the third quarter of 1997. The U.S. consumer gross margin declined from 25.4% in 1997 to 24.2% in 1998. The decline resulted from cost increases in higher volume product lines and lower manufacturing efficiencies. The medical gross margin declined $493,000 from 37.3% in 1997 to 26.8% in 1998. One third of this decline resulted from a loss of the high margin Seton products with the balance split between the loss of sales associated with a single Asian customer and lower manufacturing efficiencies. The international gross margin declined from 17.9% in 1997 to 14.9% in 1998, primarily due to Canada where lower margin products were sold from the Rotex acquisition.

Consolidated gross profit for the first nine months of 1998 was $9,109,000 (24.5% of net sales) compared with $9,950,000 (27.3% of net sales) for the first nine months of 1997. The consumer gross margin declined from 24.9% in 1997 to 25.1% in 1998. The medical gross margin declined from 38.1% in 1997 to 31.1% in 1998. The international gross margin declined from 18.8% in 1997 to 16.1% in 1998. Management expects to consolidate sourcing product from Asia to leverage its buying power to improve margins.



Selling, General and Administrative Expenses

Selling, general and administrative ("SG&A") expenses for the third quarter of 1998 were $2,737,000 (20.5% of net sales) compared with $2,925,000 (23.0% of net sales) for the same period of 1997, a decrease of $188,000, or 6%. The primary reason for the decrease was headcount reductions in all locations except Canada, partially offset by an increase in advertising expense that contributed to an increase in sales and higher commission costs that resulted from increased sales. SG&A expenses for the first nine months of 1998 of $8,133,000 (21.9% of net sales) compared with $8,742,000 (24.0% of net sales), a decrease of $609,000, or 7%. The first nine months of 1997 included $162,000 of non-recurring charges. Excluding the non-recurring charges, SG&A expense in the first nine months of 1998 declined by $528,000, or 6%, due to headcount reductions, and the elimination of certain expenses incurred in 1997 associated with the product lines sold to Seton offset by higher commissions and advertising in the consumer business associated with increased sales.

Provision for Income Taxes

The Company has tax operating loss carryforwards in the United States, England and Germany in excess of $3.4 million. The tax provision for the three and nine months periods ended September 30, 1998 was ($2,000) and $38,000, respectively, compared with $15,000 and $75,000 for the same periods for 1997. The tax provision includes minimum state and local tax obligations net of the benefit of net operating losses utilized. Management is synchronizing its manufacturing, sourcing, and tax strategies to utilize loss carryforwards.

Net Income

The Company reported net income for the third quarter of 1998 of $70,000, or 2 cents per share (diluted), compared with net income of $186,000, or 5 cents per share (diluted), for the third quarter of 1997. For the first nine months of 1998, net income was $97,000, or 3 cents per share (diluted), compared with net income of $689,000, or 19 cents per share (diluted), for the same period in 1997. The first nine months of 1997 included a gain of the sale of marketing rights to Seton offset by one-time charges; an increase in net income of $157,000 was recognized.

Financial Condition

Liquidity and Capital Resources

During the first nine months of 1998, the total debt increased by $3,052,000 compared to total debt at December 31, 1997. Of the increase, $1,698,000 was related to the Company's Acme United Limited subsidiary where a new loan agreement was negotiated in May of 1998 utilizing an asset based lending formula that provides increased working capital to support the Rotex acquisition and sales growth. The remaining increase supported capital expenditures and increased sales growth in

U.S. operations.

For the remainder of 1998, cash generated from operating activities is expected to be sufficient to reduce debt and fund capital expenditures. The Company's current credit arrangements coupled with cash expected from operating activities are considered adequate to meet liquidity needs for the remainder of 1998.

The Company's working capital, current ratio and long term debt to equity ratio follow:

| | September 30, 1998 | December 31,1997 |
|---|---|---|
| Working capital | $1,648,000 | $10,547,000 |
| Current ratio | 1.07 to 1 | 1.94 to 1 |
| Long term debt to equity ratio | .51 | 1.88 |

As of September 30, 1998, $11,780,00 is outstanding under the Company's revolving line of credit. This line matures in May of 1999. The Company is currently in negotiations with its lender to extend the maturity date and fully expects to complete such an arrangement prior to December of 1998. Had negotiations been completed during the third quarter, $13,165,00 of related debt would have been classified as long term and would have resulted in working capital of $14,813,000, a current ratio of 2.38 to 1, and long term debt to equity ratio of 2.56.



Safe Harbor for Forward-looking Statements

Except for historical information contained herein, certain statements in this Management's Discussion and Analysis of financial condition and results of operations and other sections of this document contain forward-looking statements that are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Words such as `expects,' `anticipates,' `intends,' `plans,' `believes,' `seeks,' `estimates,' or variations of such words and similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and involve unknown risks and uncertainties which may cause the Company's actual results in future periods to differ materially from forecasted results.



## PART II. OTHER INFORMATION

Item 1 - Legal Proceedings

None.

Item 2 - Changes in Securities

None.

Item 3 - Defaults Upon Senior Securities

None.

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

None.

Item 5 - Other Information

None.

Item 6 - Exhibits and Reports on Form 8-K

Form 8-K was filed by the Company on April 6, 1998, and revised on April 17, 1998.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

ACME UNITED CORPORATION

By /s/ Cheryl L. Kendall

Cheryl L. Kendall
Vice President and
Chief Financial Officer

Dated: November 11, 1998

By /s/ Richard L. Windt

Richard L. Windt
Vice President and
Corporate Controller

Dated: November 11, 1998

<ARTICLE> 5
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This schedule contains summary financial information extracted from the Condensed Consolidated Balance Sheet and Condensed Consolidated Statement of Operations and is qualified in its entirety by reference to such financial statements.
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