GANDER MOUNTAIN CO
Form 10-Q
December 16, 2008
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED NOVEMBER 1, 2008

Commission File Number: 000-50659

GANDER MOUNTAIN COMPANY
(Exact name of Registrant as Specified in its Charter)

Minnesota (State or Other Jurisdiction of Incorporation or Organization)	**180 East Fifth Street, Suite 1300** **Saint Paul, Minnesota 55101** **(651) 325-4300** (Address, including zip code, and telephone number, including area code, of Registrant s Principal Executive Offices)	**41-1990949** (I.R.S. Employer Identification No.)

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 o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. Check one:

o large accelerated filer	o accelerated filer
x non-accelerated filer (Do not check if smaller reporting company)	o smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No x

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practical date: Common Stock, $.01 par value; 24,118,755 shares outstanding as of December 2, 2008.

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QUARTERLY PERIOD ENDED NOVEMBER 1, 2008

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PART I. FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

Gander Mountain Company

Consolidated Statements of Operations - Unaudited

(In thousands, except per share data)

	13 Weeks Ended		39 Weeks Ended	
	November 1, 2008	**November 3, 2007**	**November 1, 2008**	**November 3, 2007**
Sales	$ 269,920	$ 259,539	$ 730,455	$ 651,799
Cost of goods sold	200,160	189,445	551,183	496,293
Gross profit	69,760	70,094	179,272	155,506
Operating expenses:				
Selling, general and administrative expenses	64,975	64,946	190,871	171,754
Exit costs, impairment and other charges	(1,112)	1,582	(20)	2,208
Pre-opening expenses		3,041	2,035	4,753
Income (loss) from operations	5,897	525	(13,614)	(23,209)
Interest expense, net	4,950	5,543	14,301	14,049
Income (loss) before income taxes	947	(5,018)	(27,915)	(37,258)
Income tax provision	182	125	619	375
Net Income (loss)	$ 765	$ (5,143)	$ (28,534)	$ (37,633)
Basic and diluted income (loss) per common share	$ 0.03	$ (0.25)	$ (1.18)	$ (1.86)
Weighted average common shares outstanding	24,162	20,362	24,086	20,255

See accompanying notes to unaudited consolidated financial statements.

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Gander Mountain Company

Consolidated Balance Sheets

(In thousands)

		November 1, 2008 (Unaudited)		February 2, 2008
Assets				
Current assets:				
Cash and cash equivalents	$	1,651	$	2,622
Accounts receivable		21,408		10,992
Income taxes receivable		450		486
Inventories		441,860		403,683
Prepaids and other current assets		16,554		15,987
Total current assets		481,923		433,770
Property and equipment, net		167,639		168,685
Goodwill		54,332		48,803
Acquired intangible assets, net		19,345		25,098
Other assets, net		1,985		3,576
Total assets	$	725,224	$	679,932
Liabilities and shareholders equity				
Current liabilities:				
Borrowings under credit facility	$	306,264	$	246,013
Accounts payable		88,327		72,563
Accrued and other current liabilities		48,363		60,606
Notes payable - related parties		10,000		
Current maturities of long term debt		14,077		8,247
Total current liabilities		467,031		387,429
Long term debt		56,801		64,173
Deferred income taxes		7,406		7,113
Other long term liabilities		27,476		27,397
Shareholders equity:				
Preferred stock ($.01 par value, 5,000,000 shares authorized; no shares issued and outstanding)				
Common stock ($.01 par value, 100,000,000 shares authorized; 24,118,755 and 24,049,064 shares issued and outstanding)		241		241
Additional paid-in-capital		278,334		277,110
Accumulated deficit		(112,065)		(83,531)
Total shareholders equity		166,510		193,820
Total liabilities and shareholders equity	$	725,224	$	679,932

See accompanying notes to unaudited consolidated financial statements.

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Gander Mountain Company

Consolidated Statements of Cash Flows - Unaudited

(In thousands)

	39 Weeks Ended	
	November 1, 2008	**November 3, 2007**
Operating activities		
Net loss	$ (28,534)	$ (37,633)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	23,434	19,770
Exit costs, impairment and other charges	(1,205)	
Stock-based compensation expense	989	1,278
(Gain)/ loss on disposal of assets	(62)	60
Change in operating assets and liabilities:		
Accounts receivable	(10,380)	(12,108)
Inventories	(38,177)	(122,435)
Prepaids and other current assets	(567)	(2,651)
Other assets	(121)	(1,483)
Accounts payable and other liabilities	4,786	50,407
Deferred income taxes	293	
Net cash used in operating activities	(49,544)	(104,795)
Investing activities		
Purchases of property and equipment	(16,195)	(40,548)
Acquisition of business and related expenses	(172)	(7,080)
Proceeds from sale of assets	77	
Net cash used in investing activities	(16,290)	(47,628)
Financing activities		
Borrowings under credit facility, net of repayments	60,251	139,093
Proceeds from short term notes payable - related parties	10,000	
Proceeds from long term debt		13,082
Reductions in long term debt	(5,623)	(2,463)
Proceeds from exercise of stock options and employee stock purchases	235	3,053
Net cash provided by financing activities	64,863	152,765
Net (decrease) increase in cash	(971)	342
Cash, beginning of period	2,622	1,342
Cash, end of period	$ 1,651	$ 1,684

See accompanying notes to unaudited consolidated financial statements.

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Gander Mountain Company

Notes to Unaudited Consolidated Financial Statements

Quarterly Period Ended November 1, 2008

Note 1. Basis of Presentation

The accompanying unaudited financial statements of Gander Mountain Company (we or us) have been prepared in accordance with the requirements for Form 10-Q and do not include all the disclosures normally required in annual financial statements prepared in accordance with U.S. generally accepted accounting principles. The interim financial information as of November 1, 2008 and for the 13 and 39 weeks ended November 1, 2008 and November 3, 2007, respectively, is unaudited and has been prepared on the same basis as the audited annual financial statements. In the opinion of management, this unaudited information includes all adjustments necessary for a fair presentation of the interim financial information. All of these adjustments are of a normal recurring nature. These interim financial statements filed on this Form 10-Q and the discussions contained herein should be read in conjunction with the annual financial statements and notes included in our Annual Report on Form 10-K for the fiscal year ended February 2, 2008, as filed with the Securities and Exchange Commission, which includes audited financial statements for our three fiscal years ended February 2, 2008.

Our business is seasonal in nature and interim results may not be indicative of results for a full year. Historically, we have realized more of our sales in the latter half of our fiscal year, which includes the hunting and holiday seasons. Our business is also impacted by the timing of new store openings. Both variation in seasonality and new store openings impact the analysis of the results of operations and financial condition for comparable periods.

Reclassifications - certain prior period amounts have been reclassified to conform to the current year presentation. These reclassifications had no impact on previously reported net income, cash flows or financial position.

With the acquisition of Overton s Holding Company (Overton s) in December 2007, our consolidated reporting includes our two reportable segments: Retail and Direct. The Retail segment sells its outdoor lifestyle products and services through our retail stores. The Direct segment is the internet and catalog operations under our Overton s brand name as well as the internet and catalog operations under our Gander Mountain brand, which launched August 3, 2008.

The following table shows our consolidated sales by product category for the comparable 13 week periods:

Category	**3nd Quarter 2008**	**3nd Quarter 2007**
Hunting and Firearms	51.9%	52.1%
Fishing and Marine (1)	14.1%	9.7%
Camping, Paddlesports and Backyard Equipment	6.4%	6.2%
Apparel and Footwear	21.1%	23.0%

Powersports	4.3%	6.3%
Other	1.1%	1.4%
Parts and services	1.1%	1.3%
Total	100.0%	100.0%

(1) Direct segment sales from our Overton s brand for the third quarter of fiscal 2008 have been included in the Fishing and Marine category.

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For comparative purposes, the table below reflects sales by product category for the comparable 13 week periods of our Retail segment only and does not include sales of our Direct segment.

Retail segment only **Category**	**3nd Quarter** **2008**	**3nd Quarter** **2007**
Hunting and Firearms	54.4%	52.1%
Fishing and Marine	9.9%	9.7%
Camping, Paddlesports and Backyard Equipment	6.8%	6.2%
Apparel and Footwear	22.2%	23.0%
Powersports	4.6%	6.3%
Other	1.0%	1.4%
Parts and services	1.1%	1.3%
Total	100.0%	100.0%

Note 2. Recent Accounting Pronouncements

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements.* SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. SFAS No. 157 applies to other accounting pronouncements that require or permit fair value measurements, as the FASB previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, SFAS No. 157 does not require any new fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007.

In February 2008, the FASB issued FASB Staff Position FAS 157-2, which delays the effective date for the implementation of SFAS 157 solely for non-financial assets and non-financial liabilities, except those non-financial items that are recognized at fair value in the financial statements on a recurring basis (i.e., at least annually). The effective date for non-financial assets and liabilities would be the beginning of our fiscal 2009.

We adopted SFAS No. 157 as of February 3, 2008, except as it applies to those nonfinancial assets and liabilities affected by the one-year delay. The adoption of the applicable provisions of SFAS No. 157 did not have a material impact on our results of operations, cash flows, or financial position. We do not expect the adoption of the remaining provisions of SFAS No. 157 to have a material impact on our results of operations, cash flows, or financial position.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Liabilities Including an Amendment of FASB Statement No. 115.* SFAS No. 159 permits us to choose to measure certain financial assets and liabilities at fair value that are not currently required to be measured at fair value (the Fair Value Option). Election of the Fair Value Option is made on an instrument-by-instrument basis and is irrevocable. At the adoption date, unrealized gains and losses on financial assets and liabilities for which the Fair Value Option has been elected would be reported as a cumulative adjustment to beginning retained earnings. If we elect the Fair Value Option for certain financial assets and liabilities, we will report unrealized gains and losses due to changes in their fair value in earnings at each subsequent reporting date. We adopted SFAS No. 159 but have elected not to apply the Fair Value Option of SFAS No. 159.

In December 2007, the FASB issued FAS No. 141R, *Business Combinations,* which replaces SFAS No. 141. SFAS 141R establishes principles and requirements for how the acquirer of a business recognizes and measures in its financial statements the identifiable assets acquired and the liabilities assumed. In addition, under SFAS 141(R) adjustments associated with changes in tax contingencies that occur after the one year measurement period are recorded as adjustments to income. This statement is effective for all business combinations for which the acquisition date is on or after the beginning of an entity s first fiscal year that begins after December 15, 2008; however, the guidance in this standard regarding the treatment of income tax contingencies is retrospective to business combinations completed prior to January 1, 2009. We will adopt SFAS 141(R) for any business combinations occurring at or subsequent to February 1, 2009.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities*, *an amendment of SFAS No. 133*. SFAS No. 161 is intended to improve financial standards for derivative instruments and hedging activities by requiring enhanced disclosures to enable investors to better understand the effect these instruments and activities have on an entity s financial position, financial performance and cash flows. Entities are required to provide enhanced disclosures about: how and why an entity uses derivative instruments; how derivative instruments and related hedged items are accounted for under SFAS No. 133 and its related interpretations; and how derivative instruments and related hedged items affect an entity s financial position, financial performance and cash flows. SFAS No. 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. We will adopt SFAS No. 161 beginning in the first quarter of fiscal 2009. We do not expect SFAS No. 161 to have a material impact on our results of operations, cash flows, or financial position.

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In April 2008, the FASB issued FASB Staff Position No. FAS 142-3, *Determination of the Useful Life of Intangible Assets*. FSP No. FAS 142-3 requires companies estimating the useful life of a recognized intangible asset to consider their historical experience in renewing or extending similar arrangements or, in the absence of historical experience, to consider assumptions that market participants would use about renewal or extension as adjusted for entity-specific factors. FSP No. FAS 142-3 is effective as of the beginning of our 2009 fiscal year. We are currently evaluating the potential impact, if any, of the adoption of FSP No. FAS 142-3 on our consolidated financial statements.

Note 3. Credit Facility and Indebtedness

We have maintained a revolving credit facility with Bank of America, N.A. since 2001. Our credit facility provides us with the capital to fund the operations and growth of our business. Our revolving credit facility has a limit of $345.0 million, with an option to increase this limit up to $400 million subject to certain terms and conditions. Interest on the outstanding indebtedness under the revolving portion of the credit facility currently accrues at the lender s prime commercial lending rate, or, if we elect, at the one, two, three or six month LIBOR plus 1.25% to 1.75%, depending on our EBITDA, as defined in the credit agreement. Our obligations under the credit facility are secured by interests in substantially all of the Company s assets. The credit facility matures on June 30, 2012.

In addition to the revolving credit facility, our credit facility includes a $20.0 million term loan (Term Loan A). Term Loan A matures on June 30, 2012 and bears interest at either (a) 1.25% over the higher of (i) Bank of America s prime rate or (ii) the federal funds rate plus 0.5%, or (b) LIBOR plus 2.75%.

On December 6, 2007, we entered into a Fourth Amended and Restated Loan and Security Agreement. The amendment and restatement was effected in order to add an additional $40.0 million term loan (Term Loan B) to our secured credit facility to partially fund the acquisition of Overton s. Term Loan B provides for scheduled semi-annual prepayments, beginning with $2.5 million due December 31, 2008, that fully retire the loan on its maturity date of September 30, 2011.

We will not have the ability to exercise our option to increase the revolving credit facility up to $400 million while our $40.0 million Term Loan B is outstanding.

Outstanding borrowings under the credit facility, including Term Loan A and including letters of credit, were $315.5 million and $316.2 million as of November 1, 2008 and November 3, 2007, respectively. The actual availability under the credit facility is limited to specific advance rates on eligible inventory and accounts receivable. Typically, availability will be highest in the latter half of the fiscal year as inventory levels and advance rates increase. These advance rates are seasonal as well, increasing as we approach our hunting and holiday seasons and decreasing during non-peak periods. Based on eligible inventory and accounts receivable balances as of November 1, 2008 and February 2, 2008, our available borrowing capacity under the credit facility, after subtracting letters of credit, was $35.3 million and $22.3 million, respectively.

Financial covenants under the credit facility require that availability under the line of credit not fall below 5% of the lower of the borrowing base, as defined, or the credit facility limit. This availability test is applied and measured on a daily basis. The 5% requirement increases to 7.5% in August 2009. The credit facility also contains other covenants that, among other matters, restrict our ability to incur substantial other indebtedness, create certain liens, engage in certain mergers and acquisitions, sell assets, enter into certain capital leases or make junior payments, including cash dividends. We were in compliance with all covenants as of November 1, 2008.

The value of our eligible inventory, and the related advance rates under our secured credit facility are subject to periodic adjustment based on independent valuations of our collateral performed on behalf of the banks. Any downward adjustment in the value of our inventory or in our advance rates, whether based on an assessment of the nature and quality of our inventory or a perceived increase in the difficulty of selling collateral under current economic conditions, will adversely affect our availability.

In June 2008, Bank of America, N.A. adjusted our advance rates downward, on average approximately 160 basis points, in response to general retail environment conditions. In order to maintain appropriate levels of availability under our secured credit facility, on June 9, 2008, we entered into a $10 million term loan with our two major shareholders. Amounts advanced under the agreement had an original maturity date of December 31, 2008, which was subsequently amended to March 31, 2009, bear interest at LIBOR plus 1% and may be prepaid and re-borrowed without penalty until the maturity date. The loans are unsecured and the loan agreement contains no restrictive covenants. Proceeds from the loans were used to reduce outstanding borrowings under our credit facility. The lenders under the agreement are Gratco LLC, an affiliate of

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David Pratt, our chairman and chief executive officer, and Holiday Companies, an affiliate of Ronald A. Erickson, our vice chairman, and Gerald A. Erickson, a director of our company.

Although our current expectations of future financial performance indicate that we will remain in compliance with the covenants under our credit facility, if actual financial performance does not meet our current expectations, our ability to remain in compliance with these covenants will be adversely affected. We face a number of uncertainties that may adversely affect our ability to generate sales and earnings or access any needed capital, including the recent disruption in the financial and credit markets, declining real estate values, increasing foreclosures in the housing markets, rising unemployment, and decreased business and consumer confidence that have and may continue to adversely affect discretionary spending and the retail environment in the United States.

Indebtedness- a summary of all our indebtedness is as follows:

(in thousands)	**November 1, 2008**	**February 2, 2008**
Short Term		
Borrowings under credit facility including Term Note A	**$**	