VARI LITE INTERNATIONAL INC
Form 10-Q
May 15, 2001

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 AND EXCHANGE ACT OF 1934

FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2001

COMMISSION FILE NUMBER: 0-23159

Vari-Lite International, Inc.
(Exact name of registrant as specified in its charter)

Delaware	75-2239444
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
201 Regal Row, Dallas, Texas	75247
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number including area code: (214) 630-1963

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[ ]

Indicate the number of shares outstanding of each of the Issuer's classes of common stock, as of the latest practicable date: As of May 11, 2001, there were 7,800,003 shares of Common Stock outstanding.

VARI-LITE INTERNATIONAL, INC.
INDEX TO QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED MARCH 31, 2001

VARI-LITE INTERNATIONAL, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

(IN THOUSANDS EXCEPT SHARE DATA)

ASSETS

	SEP
CURRENT ASSETS:	
Cash	$
Receivables, less allowance for doubtful accounts of $740 and $665..................	
Inventory..	
Prepaid expense and other current assets..	
TOTAL CURRENT ASSETS...	
EQUIPMENT AND OTHER PROPERTY:	
Lighting and sound equipment..	
Machinery and tools...	
Furniture and fixtures..	
Office and computer equipment...	
Work in progress and raw materials inventory..	
Less accumulated depreciation and amortization......................................	

OTHER ASSETS	
TOTAL ASSETS	$

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES:	
Accounts payable and accrued expenses	$
Unearned revenue	
Income taxes payable	
Current portion of long-term obligations	
TOTAL CURRENT LIABILITIES	
LONG-TERM OBLIGATIONS	
DEFERRED INCOME TAXES	
TOTAL LIABILITIES	
COMMITMENTS AND CONTINGENCIES (Note 8)	
STOCKHOLDERS' EQUITY:	
Preferred Stock, $0.10 par value (10,000,000 shares authorized; no shares issued)	
Common Stock, $0.10 par value (40,000,000 shares authorized; 7,845,167 shares issued; 7,800,003 shares outstanding)	
Treasury Stock	
Additional paid-in capital	
Stockholder notes receivable	
Accumulated other comprehensive income (loss) - foreign currency translation adjustment	
Retained earnings	
TOTAL STOCKHOLDERS' EQUITY	
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$

See notes to condensed consolidated financial statements.

VARI-LITE INTERNATIONAL, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

FOR THE THREE MONTHS ENDED MARCH 31, 2000 AND 2001

(UNAUDITED)

(IN THOUSANDS EXCEPT SHARE DATA)

	2000
Rental revenues	$16,432
Product sales and services revenues	4,287
TOTAL REVENUES	20,719
Rental cost	8,033

Product sales and services cost	2,450
TOTAL COST OF SALES	10,483
GROSS PROFIT	10,236
Selling, general and administrative expense	9,755
Research and development expense	1,272
TOTAL OPERATING EXPENSES	11,027
OPERATING INCOME (LOSS)	(791)
Interest expense (net)	1,260
LOSS BEFORE INCOME TAX	(2,051)
Income tax benefit	(810)
NET LOSS	(1,241)
Other comprehensive loss - foreign currency translation adjustments	(143)
COMPREHENSIVE LOSS	$ (1,384)
WEIGHTED AVERAGE BASIC AND DILUTED SHARES OUTSTANDING	7,800,003
PER SHARE INFORMATION BASIC AND DILUTED:	
Net loss	$ (0.16)

See notes to condensed consolidated financial statements.

4

VARI-LITE INTERNATIONAL, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

FOR THE SIX MONTHS ENDED MARCH 31, 2000 AND 2001

(UNAUDITED)

(IN THOUSANDS EXCEPT SHARE DATA)

	2000
Rental revenues	$40,308
Product sales and services revenues	8,090

TOTAL REVENUES	48,398
Rental cost	18,877
Product sales and services cost	4,848
TOTAL COST OF SALES	23,725
GROSS PROFIT	24,673
Selling, general and administrative expense	19,635
Research and development expense	2,467
TOTAL OPERATING EXPENSES	22,102
Gain on sale of concert sound reinforcement business	-
OPERATING INCOME	2,571
Interest expense (net)	2,520
INCOME BEFORE INCOME TAX	51
Income tax expense	20
NET INCOME	31
Other comprehensive loss - foreign currency translation adjustments	(500)
Reclassification adjustment - sale of continental European operations	-
COMPREHENSIVE INCOME (LOSS)	$ (469)
WEIGHTED AVERAGE BASIC SHARES OUTSTANDING	7,800,003
WEIGHTED AVERAGE DILUTED SHARES OUTSTANDING	7,833,682
PER SHARE INFORMATION	
BASIC AND DILUTED:	
Net income	$ 0.00

See notes to condensed consolidated financial statements.

5

VARI-LITE INTERNATIONAL, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE SIX MONTHS ENDED MARCH 31, 2000 AND 2001

(UNAUDITED)

(IN THOUSANDS)

Cash flows from operating activities:

Net income

Adjustments to reconcile net income to net cash provided by operating activities:

Depreciation and amortization

Amortization of note discount and deferred loan fees

Provision for doubtful accounts

Deferred income taxes

Gain on sale of concert sound reinforcement business

Gain on sale of equipment and other property

Net change in assets and liabilities:

Accounts receivable

Prepaid expenses

Inventory

Other assets

Accounts payable, accrued liabilities and income taxes payable

Unearned revenue

Net cash provided by (used in) operating activities

Cash flows from investing activities:

Capital expenditures, including rental equipment

Proceeds from sale of concert sound reinforcement business

Proceeds from sale of European operations

Proceeds from sale of equipment

Net cash (used in) provided by investing activities

Cash flows from financing activities:

Proceeds from issuance of debt

Principal payments on debt

Principal payments on distributor advances

Proceeds from payments on stockholder notes receivable

Net cash used in financing activities

Effect of exchange rate changes on cash and cash equivalents

Net increase (decrease) in cash during the period

Cash, beginning of period

Cash, end of period

SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid for interest expense

Cash paid for income taxes

See notes to condensed consolidated financial statements.

VARI-LITE INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

(IN THOUSANDS EXCEPT SHARE DATA)

1. Interim Financial Information

The accompanying unaudited condensed consolidated financial statements of Vari-Lite International, Inc. (the "Company") have been prepared by the Company in accordance with generally accepted accounting principles for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements.

In the opinion of management, the condensed consolidated financial statements contain all adjustments, consisting of normal recurring adjustments, considered necessary to present fairly the consolidated financial position, results of operations and cash flows of the Company. The results of operations for the three and six-month periods ended March 31, 2001 are not necessarily indicative of the results of operations that may be expected for any other interim periods or for the fiscal year ending September 30, 2001.

For further information, refer to the consolidated financial statements and accompanying notes included in the Company's Annual Report on Form 10-K for the year ended September 30, 2000. Certain prior year balances have been reclassified to conform to the current year presentation.

2. Inventory

Inventory consists of the following:

	September 30, 2000	March 31, 2001
Raw materials....................................	$12,341	$13,393
Work in progress.................................	698	685
Finished goods...................................	656	1,047
	$13,695	$15,125

3. Segment Reporting

The Company's chief operating decision maker is considered to be the Company's Chief Operating Officer ("COO"). The COO reviews financial information presented on a consolidated basis accompanied by disaggregated information about revenues by geographic region and by product lines for purposes of making operating decisions and assessing financial performance. The Company has three reportable segments: North America, Europe and Asia, which are organized, managed and analyzed geographically and operate in a single industry segment. Information about the Company's operations for the three and six-month periods ended March 31, 2000 and 2001 is presented below:

VARI-LITE INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

(IN THOUSANDS EXCEPT SHARE DATA)

	THREE M		
	NORTH AMERICA	ASIA	EUR
MARCH 31, 2000:			
Net Revenues from unaffliliated customers	$12,834	$1,563	$ 6,
Intersegment sales	5,656	-	
Total net revenues	18,490	1,563	6,
Operating income (loss)	1,534	(937)	
Depreciation and amortization	3,028	45	
Total assets	90,689	7,555	14,
MARCH 31, 2001:			
Net Revenues from unaffliliated customers	$14,679	$1,162	$ 2,
Intersegment sales	1,724	3	
Total net revenues	16,403	1,165	2,
Operating income (loss)	216	(755)	
Depreciation and amortization	1,898	44	
Total assets	68,374	8,525	15,

	SIX MONTH		
	NORTH AMERICA	ASIA	EURO
MARCH 31, 2000:			
Net Revenues from unaffliliated customers	$27,259	$5,808	$15,
Intersegment sales	10,933	-	
Total net revenues	38,192	5,808	15,
Operating income (loss)	4,116	(42)	2,
Depreciation and amortization	6,044	92	
Total assets	90,689	7,555	14,
MARCH 31, 2001:			
Net Revenues from unaffliliated customers	$27,213	$5,330	$ 6,
Intersegment sales	3,099	38	
Total net revenues	30,312	5,368	6,
Operating income	5,778	1,013	1,
Depreciation and amortization	3,876	121	1,
Total assets	68,374	8,525	15,

VARI-LITE INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

(IN THOUSANDS EXCEPT SHARE DATA)

4. Debt

On December 19, 1997, the Company entered into a $50,000 multicurrency revolving credit facility (the "Old Credit Facility") and canceled its existing credit facility. Borrowings under the Old Credit Facility were $32,200 at September 30, 2000. Subsequent to September 30, 2000, the Company used proceeds of $22,200 from the sale of the Company's concert sound reinforcement business, the sale of the Company's continental European rental operations and the funding of the London Bank Loan (hereinafter defined) to reduce borrowings under the Old Credit Facility to $10,000.

On December 29, 2000, Vari-Lite, Inc. a wholly owned subsidiary of the Company ("Vari-Lite"), entered into a three-year $24,500 credit facility (the "New Credit Facility") which includes a $12,000 term loan (the "Term Loan"), a $5,000 revolving credit facility (the "Revolver") and a $3,000 term commitment to fund capital expenditures (the "Capital Expenditure Loan"). The Revolver and the Capital Expenditure Loan commitments will increase to $7,500 and $5,000, respectively, by January 15, 2002, if the Company achieves specific financial performance. The Term Loan and Capital Expenditure Loan amortize over 84 months (subject to a balloon payment on termination of the New Credit Facility as discussed below). Borrowings under the Revolver are subject to availability under a borrowing base of eligible inventory and accounts receivable (as defined in the New Credit Facility). Initially, all outstanding borrowings under the New Credit Facility bear interest at the lender's base rate or LIBOR, plus a rate margin of .75% and 2.50%, respectively. Beginning on January 15, 2002, all outstanding balances under the New Credit Facility will bear interest at the lender's base rate or LIBOR, plus a rate margin ranging from 0.25% to 0.75% or 2.00% to 2.50%, respectively, based upon the Company's ratio of Adjusted Funded Debt to EBITDA (as defined in the New Credit Facility). The New Credit Facility is guaranteed by the Company and is secured by all of the stock and substantially all of the assets of Vari-Lite, and a pledge of 65% of the outstanding capital stock of the Company's foreign subsidiaries. A commitment fee of 0.25% is charged on the average daily unused portion of the New Credit Facility. The New Credit Facility contains compliance covenants, including requirements that the Company achieve certain financial ratios. In addition, the New Credit Facility places limitations on annual capital expenditures and on the ability to incur additional indebtedness, make certain loans or investments, sell assets, pay dividends or reacquire the Company's stock. The New Credit Facility terminates on December 31, 2003. Upon termination of the New Credit Facility, the entire outstanding indebtedness thereunder becomes due and payable in full.

On November 23, 2000, the Company entered into a British pounds sterling 4,000 (USD 5,800) term loan with a United Kingdom bank (the "London Bank Loan"). The London Bank Loan, which accrues interest at the rate of 9.1% per annum and amortizes over 48 months, is secured by all of the assets of the Company's London operations. Other terms of the London Bank

VARI-LITE INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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Loan include certain financial covenants, limitations on capital expenditures and intercompany payments and the guarantee of the Company.

The Company has borrowed money to purchase computer equipment and office furniture and fixtures and conventional lighting equipment. These loans are typically amortized over three years and bear interest at various rates ranging from 1.50% to 10.35%. Proceeds received under this type of financing were approximately $1,879 and $1,135 for the six-month periods ending March 31, 2000 and 2001, respectively, and borrowings outstanding under this type of financing at March 31, 2000 and 2001 were approximately $3,587 and $3,572, respectively.

5. Net Income Per Share

Basic earnings per share are computed based upon the weighted average number of common shares outstanding. Diluted earnings per share reflects the dilutive effect, if any, of stock options and warrants.

	Three Months ended March 31,		Six Months ended March 31,	
	2000	2001	2000	2001
Weighted average shares outstanding...	7,800,003	7,800,003	7,800,003	7,800,003
Dilutive effect of stock options and warrants after application of treasury stock method...........	-	-	33,679	71,162
Shares used in calculating diluted income per share.................	7,800,003	7,800,003	7,833,682	7,871,165

For the three-month period ended March 31, 2000 and 2001, earnings per share excludes stock options of 762,200 and 693,700, respectively, and warrants of 296,057 and 296,057, respectively, which are anti-dilutive. For the six-month period ended March 31, 2000 and 2001, earnings per share excludes stock options of 728,521 and 622,538, respectively, and 296,057 warrants which were anti-dilutive.

6. Accounting Standards Changes

In June 1998, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivative Instruments and Hedging Activities." As amended by SFAS No. 137 and SFAS No. 138, the Statement is effective for all fiscal years beginning after June 15, 2000. SFAS No. 133, as amended, establishes accounting and reporting standards for derivative instruments, including certain deriavative

instruments embedded in other contracts and for hedging activities. Under SFAS No. 133, certain contracts that were not formerly considered derivatives may now meet the definition of a derivative. The Company adopted SFAS No. 133 effective October 1, 2000. The adoption of SFAS No. 133 did not have a significant impact on the financial position or results of operations of the Company because the Company does not have significant derivative activity.

7. Dispositions

On October 26, 2000, the Company sold 100% of its interest in Vari-Lite International Europe, B.V. ("VLI Europe") and 0.4% of its interest in Vari-Lite Production Services, SAS and Vari-Lite sold all of the VARI*LITE(R) lighting equipment used in those operations. VLI Europe owned 100% of Vari-Lite Production Services, N.V., 99.6% of Vari-Lite Production Services, SAS and 100% of Vari-Lite Production Services, AB. This transaction resulted in a pre-tax charge of $3,200 which was recorded as an asset impairment in the fourth quarter of fiscal year 2000.

On November 17, 2000, the Company transferred substantially all of the assets of Showco, Inc. to Clearsho, Inc. ("Clearsho"), which assumed certain of Showco's contract liabilities, in exchange for the sole membership interest in Clearsho. On November 17, 2000, Showco sold 100% of its interest in Clearsho which resulted in a net pre-tax gain of $7,100.

8. Commitments, Contingencies and Legal Proceedings

In the ordinary course of its business, the Company is from time to time threatened with or named as a defendant in various lawsuits, including patent infringement claims. Additionally, the Company has filed lawsuits claiming infringements of its patents by third parties for which the Company has been subject to counterclaims.

In November 1999, Coemar S.p.A. and Clay Paky S.p.A. filed separate lawsuits against the Company in the United States District Court for the Southern District of New York. The suits were transferred to the United States District Court for the Northern District of Texas on July 12, 2000. The lawsuits seek declarations from the court that a certain patent of the Company is invalid, unenforceable and/or not infringed by Coemar S.p.A. and Clay Paky S.p.A. In December 2000, the Company negotiated a settlement with Coemar S.p.A. and Clay Paky S.p.A, the specific terms of which are confidential, but included a cash settlement paid to the Company and authorization for Coemar S.p.A. and Clay Paky S.p.A to continue to sell all existing products that were subject to the Company's patents. The lawsuits are currently stayed pending dismissal.

VARI-LITE INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

(IN THOUSANDS EXCEPT SHARE DATA)

9. Pro Forma Financial Statements

Pro forma adjustments to the condensed consolidated statement of operations for the three and six months ended March 31, 2000 and 2001 reflect adjustments to eliminate the results of the continental European operations sold in October 2000 and Showco sold in November 2000 (See Note 7) and the reduction of interest expense as a result of the decrease in debt. The Pro Forma Financial Statements are presented for informational purposes only and do not purport to be indicative of the results of operations that actually would have been achieved had the disposition been consummated on the financial statement date or for any future period.

	Three Months Ended March 31		Six Months Ended March 31	
	2000	2001	2000	2001
Total revenues	$16,085	$18,337	$37,366	$37,088
Total cost of sales	7,925	9,810	17,815	18,318
Gross profit	8,160	8,527	19,551	18,770
Total operating expenses	9,426	8,392	18,933	18,114
Operating income (loss)	(1,266)	135	618	656
Interest expense (net)	882	186	1,755	945
Loss before income taxes	(2,148)	(51)	(1,137)	(289)
Income tax benefit	(848)	(20)	(449)	(185)
Net loss	$(1,300)	$ (31)	$ (688)	$ (104)

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

RESULTS OF OPERATIONS

THREE MONTHS ENDED MARCH 31, 2001 COMPARED TO THREE MONTHS ENDED MARCH 31, 2000

REVENUES. Total revenues decreased 11.5%, or $2.4 million, to $18.3 million in the three-month period ended March 31, 2001, compared to $20.7 million in the three-month period ended March 31, 2000. The revenue decrease was attributable primarily to the factors set forth below.

RENTAL REVENUES. Rental revenues decreased 30.5%, or $5.0 million, to

$11.4 million in the three-month period ended March 31, 2001, compared to $16.4 million in the three-month period ended March 31, 2000. This decrease was primarily due the sale the Company's continental European rental operations in October 2000 and the sale of its concert sound reinforcement business in November 2000.

PRODUCT SALES AND SERVICES REVENUES. Product sales and services revenues increased 61.5%, or $2.6 million, to $6.9 million in the three-month period ended March 31, 2001, compared to $4.3 million in the three-month period ended March 31, 2000. This increase was primarily due to sales of new and used VARI*LITE(R) automated lighting equipment.

RENTAL COSTS. Rental cost decreased 30.6%, or $2.5 million, to $5.6 million in the three-month period ended March 31, 2001, compared to $8.0 million in the three-month period ended March 31, 2000. The decrease was primarily due to the sale of the Company's continental European rental operations in October 2000 and the sale of its concert sound reinforcement business in November 2000. Rental cost as a percentage of rental revenues in the three-month period ended March 31, 2001 was unchanged compared to the three-month period ended March 31, 2000 at 48.9%.

PRODUCT SALES AND SERVICES COSTS. Product sales and services cost increased 72.8%, or $1.8 million, to $4.2 million in the three-month period ended March 31, 2001, compared to $2.5 million in the three-month period ended March 31, 2000. Product sales and services cost as a percentage of product sales and services revenues increased to 61.2% in the three-month period ended March 31, 2001, from 57.1% in the three-month period ended March 31, 2000, primarily due to the higher costs associated with the manufacture of new automated lighting equipment sold in the three-month period ended March 31, 2001 as compared to the lower costs associated with the sale of used automated lighting equipment in the three-month period ended March 31, 2000.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSE. Selling, general and administrative expense decreased 25.9%, or $2.5 million, to $7.2 million in the three-month period ended March 31, 2001, compared to $9.8 million in the three-month period ended March 31, 2000. This expense as a percentage of total revenues decreased to 39.4% in the three-month period ended March 31, 2001, from 47.1% in the three-month period ended March 31, 2000, primarily due to the sale of the Company's continental European rental operations in October 2000, the sale of its concert sound reinforcement business in November 2000 and the closing of the Company's Hong Kong rental operations during the three-months ended March 31, 2001.

RESEARCH AND DEVELOPMENT EXPENSE. Research and development expense decreased 7.0%, or $0.1 million, to $1.2 million in the three-month period ended March 31, 2001, compared to $1.3 million in the three-month period ended March 31, 2000. This expense as a percentage of total revenues increased to 6.5% in the three-month period ended March 31, 2001, from 6.1% in the three-month period ended March 31, 2000 as a result of decreased revenues for the period ended March 31, 2001.

INTEREST EXPENSE. Interest expense decreased 61.0%, or $0.8 million, to $0.5 million in the three-month period ended March 31, 2001, compared to $1.3 million in the three-month period ended March 31, 2000 as a result of a lower debt balance and a lower interest rate in the three-month period ended March 31, 2001.

INCOME TAXES. The effective tax rate in the three-month periods ended

March 31, 2001 and 2000 were 39.1% and 39.5%, respectively.

SIX MONTHS ENDED MARCH 31, 2001 COMPARED TO SIX MONTHS ENDED MARCH 31, 2000

REVENUES. Total revenues decreased 20.0%, or $9.7 million, to $38.7 million in the six-month period ended March 31, 2001, compared to $48.4 million in the six-month period ended March 31, 2000. The revenue decrease was attributable primarily to the factors set forth below.

RENTAL REVENUES. Rental revenues decreased 27.2%, or $11.0 million, to $29.3 million in the six-month period ended March 31, 2001, compared to $40.3 million in the six-month period ended March 31, 2000. This decrease was primarily due the sale of the Company's continental European rental operations in October 2000 and the sale of its concert sound reinforcement business in November 2000 which accounted for $1.6 million of rental revenues in the six-month period ended March 31, 2001 compared to $11.0 million in the six-month period ended March 31, 2000.

PRODUCT SALES AND SERVICES REVENUES. Product sales and services revenues increased 15.9%, or $1.3 million, to $9.4 million in the six-month period ended March 31, 2001, compared to $8.1 million in the six-month period ended March 31, 2000. This increase was primarily due to the sale of new and used VARI*LITE(R) automated lighting equipment.

RENTAL COSTS. Rental cost decreased 32.4%, or $6.1 million, to $12.8 million in the six-month period ended March 31, 2001, compared to $18.9 million in the six-month period ended March 31, 2000. Rental cost as a percentage of rental revenues decreased to 43.5% in the six-month period ended March 31, 2001, from 46.8% in the six-month period ended March 31, 2000. The decrease in rental cost as a percentage of total rental revenues was primarily due to the sale of the Company's continental European operations in October 2000 and the sale of its concert sound reinforcement business in November 2000.

PRODUCT SALES AND SERVICES COSTS. Product sales and services cost increased 28.4%, or $1.4 million, to $6.2 million in the six-month period ended March 31, 2001, compared to $4.8 million in the six-month period ended March 31, 2000. Product sales and services cost as a percentage of product sales and services revenues increased to 66.4% in the six-month period ended March 31, 2001, from

59.9% in the six-month period ended March 31, 2000, primarily due to the higher costs associated with the manufacture of new automated lighting equipement sold in the six-month period ended March 31, 2001 as compared to the lower costs associated with the sale of used automated lighting equipment in the six-month period ended March 31, 2000.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSE. Selling, general and administrative expense decreased 18.0%, or $3.5 million, to $16.1 million in the six-month period ended March 31, 2001, compared to $19.6 million in the six-month period ended March 31, 2000. This decrease is primarily due to the sale of the Company's continental European rental operations in October 2000, the sale of its concert sound reinforcement business in November 2000 and the closing of the Company's Hong Kong rental operations in the six-months ended March 31, 2001. This expense as a percentage of total revenues increased to 41.6% in the six-month period ended March 31, 2001, from 40.6% in the six-month period ended March 31, 2000.

RESEARCH AND DEVELOPMENT EXPENSE. Research and development expense decreased 2.8%, or $0.1 million, to $2.4 million in the six-month period ended March 31, 2001, compared to $2.5 million in the six-month period ended March 31, 2000. This expense as a percentage of total revenues increased to 6.2% in the six-month period ended March 31, 2001, from 5.1% in the six-month period ended March 31, 2000 as a result of decreased revenues for the period ended March 31, 2000.

INTEREST EXPENSE. Interest expense decreased 38.0%, or $1.0 million, to $1.6 million in the six-month period ended March 31, 2001, compared to $2.5 million in the six-month period ended March 31, 2000 as a result of a lower debt balance and a lower interest rate in the six-month period ended March 31, 2001.

INCOME TAXES. The effective tax rate in the six-month periods ended March 31, 2001 and 2000 were 38.5% and 39.2%, respectively.

LIQUIDITY AND CAPITAL RESOURCES

Historically, the Company has financed its operations and capital expenditures with cash flow from operations, bank borrowings and advances from distributors and customers. The Company's operating activities generated cash flow of $4.1 million in the six-month period ended March 31, 2000 and used cash flow of $1.1 million for the six-month period ended March 31, 2001.

On December 19, 1997, the Company entered into the Old Credit Facility and canceled its existing credit facility. Borrowings under the Old Credit Facility were $32.2 million at September 30, 2000. Subsequent to September 30, 2000, the Company used proceeds of $22.2 million from the sale of the Company's concert sound reinforcement business, the sale of the Company's continental European rental operations and the funding of the London Bank Loan to reduce borrowings under the Old Credit Facility to $10.0 million.

On December 29, 2000, Vari-Lite entered into the New Credit Facility which includes the $12.0 Term Loan, the $5.0 million Revolver and the $3.0 million Capital Expenditure Loan. The Revolver and the Capital Expenditure Loan commitments will increase to $7.5 million and $5.0 million, respectively, by January 15, 2002, if the Company achieves specific financial performance. The Term Loan and

Capital Expenditure Loan amortize over 84 months (subject to a balloon payment on termination of the New Credit Facility as discussed below). Borrowings under the Revolver are subject to availability under a borrowing base of eligible inventory and accounts receivable (as defined in the New Credit Facility). Initially, all outstanding borrowings under the New Credit Facility bear interest at the lender's base rate or LIBOR, plus a rate margin of .75% and 2.50%, respectively. Beginning on January 15, 2002, all outstanding balances under the New Credit Facility will bear interest at the lender's base rate or LIBOR, plus a rate margin ranging from 0.25% to 0.75% or 2.00% to 2.50%, respectively, based upon the Company's ratio of Adjusted Funded Debt to EBITDA (as defined in the New Credit Facility). The New Credit Facility is guaranteed by the Company and is secured by all of the stock and substantially all of the assets of Vari-Lite, and a pledge of 65% of the outstanding capital stock of the Company's foreign subsidiaries. A commitment fee of 0.25% is charged on the average daily unused portion of the New Credit Facility. The New Credit Facility contains compliance covenants, including requirements that the Company achieve certain financial ratios. In addition, the New Credit Facility places limitations on annual capital expenditures and on the ability to incur additional indebtedness, make certain loans or investments, sell assets, pay dividends or reacquire the Company's stock. The

New Credit Facility terminates on December 31, 2003. Upon termination of the New Credit Facility, the entire outstanding indebtedness thereunder becomes due and payable in full.

On November 23, 2000, the Company entered into the British pounds sterling 4.0 million (USD 5.8 million) London Bank Loan. The London Bank Loan, which accrues interest at the rate of 9.1% per annum and amortizes over 48 months, is secured by all of the assets of the Company's London operations. Other terms of the London Bank Loan include certain financial covenants, limitations on capital expenditures and intercompany payments and the guarantee of the Company.

The Company has borrowed money to purchase computer equipment and office furniture and fixtures and conventional lighting equipment. These loans are amortized over six months to five years and bear interest at various rates ranging from 1.50% to 10.35%. Proceeds received under this type of financing were approximately $1.9 million and $1.1 million for the six-month periods ending March 31, 2000 and 2001, respectively, and borrowings outstanding under this type of financing at March 31, 2000 and 2001 were approximately $3.6 million for both years.

The Company's business requires significant capital expenditures. Capital expenditures for the six months ended March 31, 2000 and 2001 were approximately $2.3 million and $5.3 million, respectively, of which approximately $1.6 million and $4.6 million were for rental equipment inventories. The majority of the Company's revenues are generated through the rental of automated lighting systems and, as such, the Company must maintain a significant amount of rental equipment to meet customer demands.

The Company had a working capital deficit of $32.3 million at March 31, 2000 and a working capital surplus of $15.8 million at March 31, 2001. The working capital deficit at March 31, 2000 was primarily due to the scheduled maturity of the New Credit Facility on January 1, 2001, which was recorded as current debt as of March 31, 2000. The working capital surplus at March 31, 2001 is primarily the result of the refinancing of the Company's senior bank debt and the overall reduction in outstanding debt.

Management believes that cash flow generated from operations and borrowing capacity under the New Credit Facility will be sufficient to meet the Company's anticipated operating cash and capital expenditure needs for the next twelve months. Because the Company's future operating results will depend on a number of factors, including the demand for the Company's products and services, the success of the Company to market, sell and support products, the level of competition, the success of the Company's research and development programs, the Company's ability to achieve competitive and technological advances and general and economic conditions and other factors beyond the Company's control, there can be no assurance that sufficient capital resources will be available to fund the expected expansion of its business beyond such period.

DISCLOSURE REGARDING FORWARD-LOOKING STATEMENTS

This report includes "forward-looking statements" as that phrase is defined in Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. When used in this report, the words "anticipate," "believe," "estimate," "expect," "will," "could," "may" and similar expressions, as they relate to management or the Company, are intended to identify forward-looking statements. Such statements reflect the current views of management with respect to future events and are subject to certain risks, uncertainties and assumptions, including without limitation the following as they relate to the Company: fluctuations in operating results and seasonality; the success of the Company to market, sell and support products; technological changes; reliance on intellectual property; dependence on the entertainment industry; competition; dependence on management; foreign exchange risk; international trade risk; dependence on key suppliers and dependence on manufacturing facility. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those described herein.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company does not believe that the market risks for the three-month and six-month periods ended March 31, 2001 substantially changed from those risks outlined for the year ended September 30, 2000 in the Company's Form 10-K.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In the ordinary course of its business, the Company is from time to time threatened with or named as a defendant in various lawsuits, including patent infringement claims. Additionally, the Company has filed lawsuits claiming infringements of its patents by third parties for which the Company has been subject to counterclaims.

In November 1999, Coemar S.p.A. and Clay Paky S.p.A. filed separate lawsuits against the Company in the United States District Court for the Southern District of New York. The suits were transferred to the United States District Court for the Northern District of Texas on July 12, 2000. The lawsuits seek declarations from the court that a certain patent of the Company is invalid, unenforceable and/or not infringed by Coemar S.p.A. and Clay Paky S.p.A. In December 2000, the Company negotiated a settlement with Coemar S.p.A. and Clay Paky S.p.A, the specific terms of which are confidential, but included a cash settlement paid to the Company and authorization for Coemar S.p.A. and Clay Paky S.p.A to continue to sell all existing products that were subject to the Company's patents. The lawsuits are currently stayed pending dismissal.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

On March 2, 2001, the Annual Meeting of Stockholders was held in Dallas, Texas. The stockholders were asked to elect one Class I director to serve until 2004. The vote was as follows:

	For	Against or Withheld	Abstentions
John D. Maxson	6,676,782	34,830	1,088,391

Messrs. Brutsche', Clark, Rettberg and Smith will continue as directors of the Company. Subsequent to the Annual Meeting of Stockholders on March 2, 2001, the Company's Board of Directors appointed Jon Tinkle and

William Scott to serve as directors of the Company.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

10.58	Employment Agreement, dated January 1, 2001, between the Company and T. Clay Powers
10.59	Employment Agreement, dated January 1, 2001 , between the Company and Jerome L. Trojan III

(b) No reports on Form 8-K were filed for the quarter ended March 31, 2001.

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.

VARI-LITE INTERNATIONAL, INC.

Date: MAY 11, 2001

By: /s/ JEROME L. TROJAN III

Jerome L. Trojan III
Vice President - Finance,
Chief Financial Officer, Treasurer
and Secretary (Principal Financial
and Accounting Officer)