

CHAMPION INDUSTRIES INC  
Form 10-Q  
March 11, 2005

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, DC 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  
January 31, 2005

Commission File No.  
0-21084

---

**Champion Industries, Inc.**

(Exact name of Registrant as specified in its charter)

West Virginia  
(State or other jurisdiction of  
incorporation or  
organization)

55-0717455  
(I.R.S. Employer  
Identification No.)

2450-90 1<sup>st</sup> Avenue  
P.O. Box 2968  
Huntington, WV 25728  
(Address of principal executive offices)  
(Zip Code)

(304) 528-2700  
(Registrant's telephone number,  
including area code)

---

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  No .

Edgar Filing: CHAMPION INDUSTRIES INC - Form 10-Q

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).  
Yes \_\_\_ No ü.

9,733,913 shares of common stock of the Registrant were outstanding at January 31, 2005.

---

**Champion Industries, Inc.**

**INDEX**

	<b>Page No.</b>
<b>Part I. Financial Information</b>	
<b>Item 1. Financial Statements</b>	
Consolidated Balance Sheets (Unaudited)	3
Consolidated Statements of Income (Unaudited)	5
Consolidated Statements of Cash Flows (Unaudited)	6
Notes to Consolidated Financial Statements	7
<b>Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations</b>	13
<b>Item 3a. Quantitative and Qualitative Disclosure About Market Risk</b>	16
<b>Item 4. Controls and Procedures</b>	16
<b>Part II. Other Information</b>	
<b>Item 6. Exhibits</b>	17
<b>Signatures</b>	18

**PART I - FINANCIAL INFORMATION****Item 1. Financial Statements****Champion Industries, Inc. and Subsidiaries  
Consolidated Balance Sheets**

<b>ASSETS</b>	<b>January 31, 2005 (Unaudited)</b>	<b>October 31, 2004 (Audited)</b>
Current assets:		
Cash and cash equivalents	\$ 4,340,042	\$ 1,745,457
Accounts receivable, net of allowance of \$1,437,000 and \$1,422,000	17,965,402	21,318,016
Inventories	11,098,798	11,269,514
Other current assets	1,432,573	973,832
Deferred income tax assets	1,144,943	1,144,943
Total current assets	35,981,758	36,451,762
Property and equipment, at cost:		
Land	2,006,375	2,006,375
Buildings and improvements	8,319,543	8,253,573
Machinery and equipment	43,770,959	43,228,587
Equipment under capital leases	983,407	983,407
Furniture and fixtures	3,431,688	3,361,100
Vehicles	3,581,435	3,523,467
	62,093,407	61,356,509
Less accumulated depreciation	(41,978,613)	(41,020,327)
	20,114,794	20,336,182
Cash surrender value of officers' life insurance	1,039,514	1,039,514
Goodwill	2,060,786	2,060,786
Other intangibles, net of accumulated amortization	3,726,571	3,812,051
Other assets	333,064	449,589
	7,159,935	7,361,940
Total assets	\$ 63,256,487	\$ 64,149,884

See notes to consolidated financial statements.

**Champion Industries, Inc. and Subsidiaries**  
**Consolidated Balance Sheets (continued)**

<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>	<b>January 31, 2005 (Unaudited)</b>	<b>October 31, 2004 (Audited)</b>
<b>Current liabilities:</b>		
Accounts payable	\$ 3,926,215	\$ 3,618,051
Accrued payroll	1,374,739	1,778,736
Taxes accrued and withheld	1,408,691	1,289,524
Accrued income taxes	310,897	135,556
Accrued expenses	1,097,807	1,028,246
<b>Current portion of long-term debt:</b>		
Notes payable	1,567,630	1,555,911
Capital lease obligations	94,020	132,518
<b>Total current liabilities</b>	<b>9,779,999</b>	<b>9,538,542</b>
<b>Long-term debt, net of current portion:</b>		
Notes payable, line of credit	1,800,000	2,300,000
Notes payable, term	5,544,696	5,940,323
Capital lease obligations	-	16,484
Other liabilities	429,192	428,366
Deferred income tax liabilities	4,375,357	4,375,357
<b>Total liabilities</b>	<b>21,929,244</b>	<b>22,599,072</b>
<b>Commitments and contingencies</b>		
<b>Shareholders' equity:</b>		
Common stock, \$1 par value, 20,000,000 shares authorized;		
9,733,913 shares issued and outstanding	9,733,913	9,733,913
Additional paid-in capital	22,278,110	22,278,110
Retained earnings	9,315,220	9,538,789
<b>Total shareholders' equity</b>	<b>41,327,243</b>	<b>41,550,812</b>
	\$	\$
<b>Total liabilities and shareholders' equity</b>	<b>63,256,487</b>	<b>64,149,884</b>

See notes to consolidated financial statements.

**Champion Industries, Inc. and Subsidiaries**  
**Consolidated Statements of Income**  
(Unaudited)

	<b>Three Months Ended January 31,</b>	
	<b>2005</b>	<b>2004</b>
Revenues:		
	\$	\$
Printing	<b>24,436,621</b>	22,997,892
Office products and office furniture	<b>10,003,370</b>	6,315,581
Total revenues	<b>34,439,991</b>	29,313,473
Cost of sales:		
Printing	<b>17,877,263</b>	17,023,500
Office products and office furniture	<b>7,004,263</b>	4,324,101
Total cost of sales	<b>24,881,526</b>	21,347,601
Gross profit	<b>9,558,465</b>	7,965,872
Selling, general and administrative expenses	<b>9,025,372</b>	7,921,054
Income from operations	<b>533,093</b>	44,818
Other income (expense):		
Interest income	<b>5,066</b>	1,618
Interest expense	<b>(137,365)</b>	(46,679)
Other	<b>62,673</b>	23,034
	<b>(69,626)</b>	(22,027)
Income before income taxes	<b>463,467</b>	22,791
Income tax expense	<b>(200,341)</b>	(9,178)
Net income	<b>\$ 263,126</b>	\$ 13,613
Earnings per share:		
Basic	<b>\$ 0.03</b>	\$ 0.00
Diluted	<b>\$ 0.03</b>	\$ 0.00
Weighted average shares outstanding:		
Basic	<b>9,734,000</b>	9,717,000
Diluted	<b>9,802,000</b>	9,826,000
Dividends per share	<b>\$ 0.05</b>	\$ 0.05

See notes to consolidated financial statements.

**Champion Industries, Inc. and Subsidiaries**  
**Consolidated Statements of Cash Flows**  
(Unaudited)

	<b>Three Months Ended January 31,</b>	
	<b>2005</b>	<b>2004</b>
<b>Cash flows from operating activities:</b>		
Net income	\$ 263,126	\$ 13,613
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation and amortization	1,152,111	975,126
Gain on sale of assets	(4,099)	(1,107)
Increase in deferred compensation	1,787	2,681
Bad debt expense	114,224	124,209
Changes in assets and liabilities:		
Accounts receivable	3,238,390	3,192,173
Inventories	170,716	397,129
Other current assets	(458,741)	(488,819)
Accounts payable	308,164	(845,735)
Accrued payroll	(403,997)	(536,191)
Taxes accrued and withheld	119,167	(125,986)
Income taxes	175,341	(612,180)
Accrued expenses	69,561	(137,423)
Other liabilities	(961)	(3,735)
Net cash provided by operating activities	4,744,789	1,953,755
<b>Cash flows from investing activities:</b>		
Purchases of property and equipment	(855,535)	(1,009,258)
Proceeds from sales of property	24,223	58,064
Goodwill additions	—	(130,814)
Decrease in cash surrender value life insurance	—	32,661
Other assets	106,693	25,594
Net cash used in investing activities	(724,619)	(1,023,753)
<b>Cash flows from financing activities:</b>		
Borrowings on line of credit	993,000	1,000,000
Payments on line of credit	(1,493,000)	(705,668)
Principal payments on long-term debt	(438,890)	(266,985)
Proceeds from exercise of stock options	—	10,520
Dividends paid	(486,695)	(485,897)
Net cash used in financing activities	(1,425,585)	(448,030)
Net increase in cash and cash equivalents	2,594,585	481,972
Cash and cash equivalents, beginning of period	1,745,457	2,171,713
Cash and cash equivalents, end of period	\$ 4,340,042	\$ 2,653,685

See notes to consolidated financial statements.

**Champion Industries, Inc. and Subsidiaries****Notes to Consolidated Financial Statements (Unaudited)****January 31, 2005****1. Basis of Presentation and Business Operations**

The foregoing financial information has been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") and rules and regulations of the Securities and Exchange Commission for interim financial reporting. The preparation of the financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates. In the opinion of management, the financial information reflects all adjustments (consisting of items of a normal recurring nature) necessary for a fair presentation of financial position, results of operations and cash flows in conformity with GAAP. These interim financial statements should be read in conjunction with the consolidated financial statements for the year ended October 31, 2004, and related notes thereto contained in Champion Industries, Inc.'s Form 10-K dated January 17, 2005. The accompanying interim financial information is unaudited. The balance sheet information as of October 31, 2004 was derived from our audited financial statements.

**2. Earnings per Share**

Basic earnings per share is computed by dividing net income by the weighted average shares of common stock outstanding for the period and excludes any dilutive effects of stock options. Diluted earnings per share is computed by dividing net income by the weighted average shares of common stock outstanding for the period plus the shares that would be outstanding assuming the exercise of dilutive stock options. The dilutive effect of stock options was 68,000 and 109,000 shares for the three months ended January 31, 2005 and 2004.

**3. Inventories**

Inventories are principally stated at the lower of first-in, first-out cost or market. Manufactured finished goods and work in process inventories include material, direct labor and overhead based on standard costs, which approximate actual costs. The Company utilizes an estimated gross profit method for determining cost of sales in interim periods.

Inventories consisted of the following:

	<b>January 31, 2005</b>	<b>October 31, 2004</b>
Printing:		
Raw materials	\$ 2,395,965	\$ 2,326,821
Work in process	2,058,221	1,998,824
Finished goods	3,563,676	3,460,834
Office products and office furniture	3,080,936	3,483,035
	<b>\$ 11,098,798</b>	<b>\$ 11,269,514</b>



**Champion Industries, Inc. and Subsidiaries**  
**Notes to Consolidated Financial Statements (Unaudited) (continued)**

**4. Long-Term Debt**

Long-term debt consisted of the following:

	January 31, 2005	October 31, 2004
Secured term note payable	\$ 3,698,242	\$ 3,920,000
Installment notes payable to banks	3,414,084	3,576,234
Capital lease obligations	94,020	149,002
	7,206,346	7,645,236
Less current portion	1,661,650	1,688,429
Long-term debt, net of current portion	\$ 5,544,696	\$ 5,956,807

The Company has an unsecured revolving line of credit with a bank for borrowings to a maximum of \$10,000,000 with interest payable monthly at the prime rate of interest. The line of credit expires in July 2006 and contains certain restrictive financial covenants. The Company had outstanding borrowings under this facility of \$1.8 million and \$2.3 million at January 31, 2005 and October 31, 2004.

The Company has an unsecured revolving line of credit with a bank for borrowings to a maximum of \$1,000,000 with interest payable monthly at the Wall Street Journal prime rate. The line of credit expires in October 2005 and contains certain financial covenants. There were no borrowings outstanding under this facility at January 31, 2005 and October 31, 2004.

There were no non-cash financing activities for the three months ended January 31, 2005 and 2004.

**5. Shareholders' Equity**

The Company paid a dividend of five cents per share on December 31, 2004 to stockholders of record on December 3, 2004. Also, the Company declared a dividend of five cents per share to be paid on March 28, 2005 to stockholders of record on March 11, 2005.

**6. Commitments and Contingencies**

On February 16, 2002, a jury verdict was rendered against the Company in a civil action brought against the Company in state court in Jackson, Mississippi. The plaintiff in this civil action asserted that the Company and its Dallas Printing Company, Inc. subsidiary had engaged in unfair competition and other wrongful acts in hiring certain of its employees. The jury awarded the plaintiff \$1,745,000 in actual damages and \$750,000 in punitive damages.

On March 1, 2002, the plaintiff filed a motion for attorney's fees and costs in the amount of \$889,401. On July 16, 2002, the court entered an order granting plaintiff \$645,119 in attorney fees and expenses, and ordered that interest on the amount of the jury award accrue from February 22, 2002.

The Company appealed both the jury award and the attorney fee and expense award.

**Champion Industries, Inc. and Subsidiaries**  
**Notes to Consolidated Financial Statements (Unaudited) (continued)**

The Company was advised on February 3, 2004 that the Court of Appeals of the State of Mississippi had reversed the aforementioned judgment and jury verdict rendered against the Company and had remanded the case for new trial. The plaintiff petitioned the appeals court for rehearing of its ruling on February 17, 2004. The Company's response was filed on February 24, 2004.

On June 22, 2004 the Company was advised that the Court of Appeals of the State of Mississippi had upheld its February 3, 2004 reversal of the judgment and jury verdict and its remand of the case for new trial and had denied plaintiff's petition for rehearing of that decision. Plaintiff filed a petition for writ of certiorari with the Mississippi Supreme Court to contest the ruling of the Court of Appeals on July 6, 2004. The Company filed a response to such petition on July 27, 2004.

The Company was advised on September 16, 2004 that the Supreme Court of Mississippi had upheld the Court of Appeals of the State of Mississippi's February 3, 2004 reversal of the judgment and jury verdict rendered February 16, 2002 against the Company and had upheld the reversal and remand of the case for new trial.

The effect of the appeals courts orders of February 3, 2004 and June 22, 2004 and the Mississippi Supreme Court's denial of plaintiff's petition for certiorari is to negate the trial court's award of damages and attorneys fees previously granted against the Company, and grant a new trial on plaintiff's claims.

As of January 31, 2005 the Company had contractual obligations in the form of leases and debt as follows:

<b>Contractual Obligations</b>	<b>Payments Due by Fiscal Year</b>						<b>Total</b>
	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>Residual</b>	
Non-cancelable operating leases	\$ 1,047,867	\$ 1,220,998	\$ 945,183	\$ 701,474	\$ 253,340	\$ -	\$ 4,168,862
Revolving line of credit	-	1,800,000	-	-	-	-	1,800,000
Term debt	1,172,003	1,561,364	1,580,206	1,583,979	300,328	914,446	7,112,326
Obligations under capital leases	77,536	16,484	-	-	-	-	94,020
	\$ 2,297,406	\$ 4,598,846	\$ 2,525,389	\$ 2,285,453	\$ 553,668	\$ 914,446	\$ 13,175,208

## **7. Accounting for Stock-Based Compensation**

In December 2004, the FASB issued SFAS No. 123R (revised 2004), *Share-Based Payment*. This statement revises SFAS No. 123, *Accounting for Stock-Based Compensation*, and requires companies to expense the value of employee stock options and similar awards. The effective date of this standard is interim and annual periods beginning after June 15, 2005.

The Company has elected to follow the intrinsic value method in accounting for its employee stock options. Accordingly, because the exercise price of the Company's employee stock options equals the market price of the underlying stock on the date of grant, no compensation expense is recognized.



**Champion Industries, Inc. and Subsidiaries**  
**Notes to Consolidated Financial Statements (Unaudited) (continued)**

The fair value of these options was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted-average assumptions for 2004, risk-free interest rates of 4.03%, dividend yields of 4.21%, volatility factors of the expected market price of the Company's common stock of 54.0% and a weighted-average expected life of the option of 4 years.

The following pro forma information has been determined as if the Company had accounted for its employee stock options under the fair value method. For purposes of pro forma disclosures, the estimated fair value of the options is expensed in the year granted since the options vest immediately. The Company's pro forma information for the quarters ended January 31 are as follows:

	<b>Quarter Ended January 31,</b>	
	<b>2005</b>	<b>2004</b>
Net income, as reported	\$ 263,126	\$ 13,613
Deduct: Total stock-based employee compensation expense determined under fair value method for all awards, net of related tax effects	-	109,962
Pro forma net income (loss)	\$ 263,126	\$ (96,349)
Earnings (loss) per share:		
Basic, as reported	\$ 0.03	\$ 0.00
Basic, pro forma	0.03	(0.01)
Diluted, as reported	\$ 0.03	\$ 0.00
Diluted, pro forma	0.03	(0.01)

Since the Company had a pro-forma net loss as shown above for the three months ended January 31, 2004 the dilutive effect of 109,000 stock options were anti-dilutive on a pro-forma basis for the three months ended January 31, 2004.

## 8. Acquisitions

On September 7, 2004 the Company acquired all the issued and outstanding capital stock of Syscan Corporation ("Syscan"), a West Virginia corporation, for a cash price of \$3,500,000 and a contingent purchase price, dependent upon satisfaction of certain conditions, not to exceed the amount of \$1,500,000.

The Williams Land Corporation has the option to put the 3000 Washington Street building occupied by Syscan to the Company for a price of \$1.5 million and the Company has the option to purchase the building for \$1.5 million at the conclusion of the five year lease term commencing September 1, 2009. This option may be exercised no later than 60 days prior to the end of the lease and closing of said purchase cannot exceed 45 days for the end of the lease.

**Champion Industries, Inc. and Subsidiaries**  
**Notes to Consolidated Financial Statements (Unaudited) (continued)**

**9. Industry Segment Information**

The Company operates principally in two industry segments organized on the basis of product lines: the production, printing and sale, principally to commercial customers, of printed materials (including brochures, pamphlets, reports, tags, continuous and other forms), and the sale of office products and office furniture including interior design services.

The table below presents information about reported segments for the three months ended January 31:

	<b>O f f i c e Products &amp; Furniture</b>		
<b>2005 Quarter 1</b>	<b>Printing</b>	<b>&amp; Furniture</b>	<b>Total</b>
Revenues	\$ 28,085,977	\$ 11,528,769	\$ 39,614,746
Elimination of intersegment revenue	(3,649,356)	(1,525,399)	(5,174,755)
Consolidated revenues	\$ 24,436,621	\$ 10,003,370	\$ 34,439,991
Operating income	271,729	261,364	533,093
Depreciation & amortization	1,072,454	79,657	1,152,111
Capital expenditures	782,748	72,787	855,535
Identifiable assets	53,108,233	10,148,254	63,256,487
Goodwill	1,774,344	286,442	2,060,786
	<b>Office Products &amp; Furniture</b>		
<b>2004 Quarter 1</b>	<b>Printing</b>	<b>Furniture</b>	<b>Total</b>
Revenues	\$ 25,530,021	\$ 7,689,954	\$ 33,219,975
Elimination of intersegment revenue	(2,532,129)	(1,374,373)	(3,906,502)
Consolidated revenues	\$ 22,997,892	\$ 6,315,581	\$ 29,313,473
Operating income (loss)	177,384	(132,566)	44,818
Depreciation & amortization	961,696	13,430	975,126
Capital expenditures	993,549	15,709	1,009,258
Identifiable assets	45,995,910	9,779,939	55,775,849

Goodwill	1,774,344	286,442	2,060,786
----------	-----------	---------	-----------

**Champion Industries, Inc. and Subsidiaries**  
**Notes to Consolidated Financial Statements (Unaudited) (continued)**

A reconciliation of total segment revenues and of total segment operating income to income before income taxes, for the three months ended January 31, 2005 and 2004, is as follows:

	<b>Three Months Ended January 31,</b>	
	<b>2005</b>	<b>2004</b>
<b>Revenues:</b>		
Total segment revenues	\$ 39,614,746	\$ 33,219,975
Elimination of intersegment revenue	(5,174,755)	(3,906,502)
<b>Consolidated revenue</b>	<b>\$ 34,439,991</b>	<b>\$ 29,313,473</b>
<b>Operating income:</b>		
Total segment operating income	\$ 533,093	\$ 44,818
Interest income	5,066	1,618
Interest expense	(137,365)	(46,679)
Other income	62,673	23,034
<b>Consolidated income before income taxes</b>	<b>\$ 463,467</b>	<b>\$ 22,791</b>
<b>Identifiable assets:</b>		
Total segment identifiable assets	\$ 63,256,487	\$ 55,775,849
Elimination of intersegment assets	—	—
<b>Total consolidated assets</b>	<b>\$ 63,256,487</b>	<b>\$ 55,775,849</b>

**Champion Industries, Inc. and Subsidiaries**

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

**Results of Operations**

The following table sets forth, for the periods indicated, information derived from the Consolidated Income Statements as a percentage of total revenues.

	Three Months Ended January 31,			
	2005		2004	
	(\$ in thousands)			
<b>Revenues:</b>				
Printing	\$ 24,437	71.0%	\$ 22,998	78.5%
Office products and office furniture	10,003	29.0	6,316	21.5
<b>Total revenues</b>	<b>34,440</b>	<b>100.0</b>	29,314	100.0
<b>Cost of sales:</b>				
Printing	17,878	51.9	17,024	58.1
Office products and office furniture	7,004	20.3	4,324	14.7
<b>Total cost of sales</b>	<b>24,882</b>	<b>72.2</b>	21,348	72.8
<b>Gross profit</b>	<b>9,558</b>	<b>27.8</b>	7,966	27.2
Selling, general and administrative expenses	9,025	26.2	7,921	27.0
<b>Income from operations</b>	<b>533</b>	<b>1.6</b>	45	0.2
Interest income	5	0.0	2	0.0
Interest expense	(137)	(0.4)	(47)	(0.1)
Other income	62	0.2	23	0.0
<b>Income before taxes</b>	<b>463</b>	<b>1.4</b>	23	0.1
Income taxes	(200)	(0.6)	(9)	(0.0)
<b>Net income</b>	<b>\$ 263</b>	<b>0.8%</b>	\$ 14	0.1%

**Three Months Ended January 31, 2005 Compared to Three Months Ended January 31, 2004**

*Revenues*

Total revenues increased 17.5% in the first quarter of 2005 compared to the same period in 2004 from \$29.3 million to \$34.4 million. Printing revenue increased 6.3% in the first quarter of 2005 to \$24.4 million from \$23.0 million in the first quarter of 2004. Office products and office furniture revenue increased 58.4% in the first quarter of 2005 to \$10.0 million from \$6.3 million in the first quarter of 2004. The revenue increase for the office products and office furniture segment was attributable to an increase in furniture sales in 2005 due in part to the additional sales derived from the purchase of Syscan coupled with organic growth and additional office product sales resulting from the Syscan acquisition. The increase in printing sales was primarily due to additional sales derived from the Syscan acquisition.



**Champion Industries, Inc. and Subsidiaries**

**Management's Discussion and Analysis of Financial Condition  
and Results of Operations (continued)**

*Cost of Sales*

Total cost of sales increased 16.6% in the first quarter of 2005 to \$24.9 million from \$21.3 million in the first quarter of 2004. Printing cost of sales in the first quarter of 2005 increased \$854,000 over the prior year and decreased as a percentage of printing sales from 74.0% in 2004 to 73.2% in 2005 primarily due to improved market pricing integrity. The printing gross margin dollar increase resulted from both increased sales volume and improved market pricing integrity. Office products and office furniture cost of sales increased 62.0% or approximately \$2.7 million in 2005 to \$7.0 million from \$4.3 million in 2004 and increased as a percent of sales from 68.5% in 2004 to 70.0% in 2005. The increase in office products and office furniture cost of sales is attributable to the increase in sales. The increase in office products and office furniture cost of sales as a percent of sales is reflective of decreased margins due in part to wholesale pricing factors at Syscan for office supplies.

*Operating Expenses*

In the first quarter of 2005, selling, general and administrative expenses increased on a gross dollar basis to \$9.0 million from \$7.9 million in 2004, an increase of \$1.1 million or 13.9%. As a percentage of sales the expenses decreased on a quarter to quarter basis in 2005 to 26.2% from 27.0% in 2004 of total sales.

The increase in selling, general and administrative expenses is primarily the result of additional costs incurred as a result of the acquisition of Syscan in September 2004.

*Income from Operations and Other Income and Expenses*

Income from operations increased in the first quarter of 2005 to \$533,000 from \$45,000 in the first quarter of 2004. This increase is the result of increased sales and gross profit, coupled with a decrease in selling, general and administrative expenses as a percent of sales. Other expense (net), increased approximately \$48,000 from 2004 to 2005 primarily due to increases in interest expense resulting from higher outstanding borrowings and increased interest rates.

*Income Taxes*

The Company's effective income tax rate was 43.2% for the first quarter of 2005 and 40.3% for the first quarter of 2004. The increase in income taxes as a percentage of income before taxes is primarily related to the nondeductibility of certain selling related expenses. The effective income tax rate approximates the combined federal and state, net of federal benefit, statutory income tax rate.

*Net Income*

Net income for the first quarter of 2005 was \$263,000 compared to net income of \$14,000 in the first quarter of 2004. Basic and diluted earnings per share for the three months ended January 31, 2005 and 2004 were \$0.03 and \$0.00.

**Inflation and Economic Conditions**

Management believes that the effect of inflation on the Company's operations has not been material and will continue to be immaterial for the foreseeable future. The Company does not have long-term sales



**Champion Industries, Inc. and Subsidiaries**

**Management's Discussion and Analysis of Financial Condition  
and Results of Operations (continued)**

and purchase contracts; therefore, to the extent permitted by competition, it has the ability to pass through to the customer most cost increases resulting from inflation, if any.

**Seasonality**

Historically, the Company has experienced a greater portion of its profitability in the second and fourth quarters than in the first and third quarters. The second quarter generally reflects in-creased orders for printing of corporate annual reports and proxy statements. A post-Labor Day increase in demand for printing services and office products coincides with the Company's fourth quarter.

**Liquidity and Capital Resources**

Net cash provided by operations for the three months ended January 31, 2005, was \$4.7 million compared to net cash provided by operations of \$2.0 million during the same period in 2004. This change in net cash from operations is due primarily to timing changes in assets and liabilities, including an increase in accounts payable in 2005 compared to a decrease in accounts payable in 2004 and additional tax payments during the first quarter of 2004 compared to the first quarter of 2005.

Net cash used in investing activities for the three months ended January 31, 2005 was \$725,000 compared to \$1.0 million during the same period in 2004. The net cash used in investing activities during the first three months of 2005 primarily relates to equipment and vehicle purchases and for the first three months of 2004 primarily relates to equipment, vehicle purchases and building improvements.

Net cash used in financing activities for the three months ended January 31, 2005 was \$1.4 million compared to \$448,000 during the same period in 2004. This change is primarily due to net payments on the Company's line of credit of \$500,000 compared with net borrowings of approximately \$300,000 in 2004 and a \$172,000 increase in principal payments in 2005 on term debt.

The Company's off balance sheet arrangements at January 31, 2005 relate to the Syscan acquisition and are associated with potential contingent purchase price consideration of \$1.5 million payable in October 2006 and a put option from Williams Land Corporation to sell a building to the Company for \$1.5 million. This option may be exercised no later than 60 days prior to the end of the lease and closing of said purchase cannot exceed 45 days from the end of the lease. The lease term concludes effective September 1, 2009.

Working capital on January 31, 2005 was \$26.2 million, a decrease of \$700,000 from October 31, 2004. Management believes that working capital and operating ratios remain at acceptable levels.

The Company expects that the combination of funds available from working capital, borrowings available under the Company's credit facilities and anticipated cash flows from operations will provide sufficient capital resources for the foreseeable future. In the event the Company seeks to accelerate internal growth or make acquisitions beyond these sources, additional financing would be necessary.

**Environmental Regulation**

The Company is subject to the environmental laws and regulations of the United States, and the states in which it operates, concerning emissions into the air, discharges into the waterways and the generation,

15

---

**Champion Industries, Inc. and Subsidiaries**

**Management's Discussion and Analysis of Financial Condition  
and Results of Operations (continued)**

handling and disposal of waste materials. The Company's past expenditures relating to environmental compliance have not had a material effect on the Company. These laws and regulations are constantly evolving, and it is impossible to predict accurately the effect they may have upon the capital expenditures, earnings, and competitive position of the Company in the future. Based upon information currently available, management believes that expenditures relating to environmental compliance will not have a material impact on the financial position of the Company.

**Special Note Regarding Forward-Looking Statements**

Certain statements contained in this Form 10-Q, including without limitation statements including the word "believes," "anticipates," "intends," "expects" or words of similar import, constitute "forward-looking statements" within the meaning of section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements of the Company expressed or implied by such forward-looking statements. Such factors include, among others, general economic conditions, changes in business strategy or development plans, and other factors referenced in this Form 10-Q. Given these uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements. The Company disclaims any obligation to update any such factors or to publicly announce the results of any revisions to any of the forward-looking statements contained herein to reflect future events or developments.

**ITEM 3a. Quantitative and Qualitative Disclosure About Market Risk**

The Company does not have any significant exposure relating to market risk.

**ITEM 4. Controls and Procedures**

Company management, including the Chief Executive Officer, Chief Operating Officer and Chief Financial Officer, has conducted an evaluation of the effectiveness of disclosure controls and procedures pursuant to Exchange Act Rule 13a-15c as of the end of the period covered by this quarterly report. Based on that evaluation, the Chief Executive Officer, Chief Operating Officer and Chief Financial Officer concluded that the disclosure controls and procedures are effective in ensuring that all material information required to be filed in this quarterly report has been made known to them in a timely fashion. There were no changes in internal controls over financial reporting during the last fiscal quarter that have materially affected or are reasonably likely to materially affect the Company's internal controls over financial reporting.

**PART II - OTHER INFORMATION**

**Item 6. Exhibits**

a)

Exhibits:

- (31.1) Principal Executive Officer                      Exhibit 31.1 Page Exhibit 31.1-p1  
Certification Pursuant to Section 302  
of the Sarbanes-Oxley act of 2002 -  
Marshall T. Reynolds
  
- (31.2) Principal Financial Officer                      Exhibit 31.2 Page Exhibit 31.2-p1  
Certification Pursuant to Section 302  
of the Sarbanes-Oxley act of 2002 -  
Todd R. Fry
  
- (31.3) Principal Operating Officer                      Exhibit 31.3 Page Exhibit 31.3-p1  
Certification Pursuant to Section 302  
of the Sarbanes-Oxley act of 2002 -  
Toney K. Adkins
  
- (32) Marshall T. Reynolds, Todd R. Fry              Exhibit 32 Page Exhibit 32-p1  
and Toney K. Adkins Certification  
Pursuant to 18 U.S.C. Section 1350 as  
Adopted Pursuant to Section 906 of  
the Sarbanes-Oxley act of 2002

**SIGNATURES**

Pursuant to the requirement 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.

CHAMPION INDUSTRIES, INC.

Date: March 11, 2005

/s/ Marshall T. Reynolds  
Marshall T. Reynolds  
Chief Executive Officer

Date: March 11, 2005

/s/ Toney K. Adkins  
Toney K. Adkins  
President and Chief Operating Officer

Date: March 11, 2005

/s/ Todd R. Fry  
Todd R. Fry  
Senior Vice President and Chief Financial  
Officer

