NATIONAL SERVICE INDUSTRIES INC
Form 10-Q
January 09, 2001

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended November 30, 2000.

OR

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

For the transition period from __________________ to ____________________.

Commission file number 1-3208.

NATIONAL SERVICE INDUSTRIES, INC.
(Exact name of registrant as specified in its charter)

Delaware	58-0364900
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

1420 Peachtree Street, N.E., Atlanta, Georgia 30309-3002
(Address of principal executive offices) (Zip Code)

(404) 853-1000
(Registrant's telephone number, including area code)

None
(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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.

Common Stock - $1.00 Par Value - 41,052,654 shares as of December 31, 2000

NATIONAL SERVICE INDUSTRIES, INC. AND SUBSIDIARIES

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NATIONAL SERVICE INDUSTRIES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS (Unaudited)
(In thousands, except share and per-share data)

	Novem 2
ASSETS	
Current Assets:	
Cash and cash equivalents	
Receivables, less reserves for doubtful accounts of $8,269 at November 30, 2000 and $7,310 at August 31, 2000	
Inventories, at the lower of cost (on a first-in, first-out basis) or market	
Linens in service, net of amortization	
Deferred income taxes	
Prepayments	
Total Current Assets	
Property, Plant, and Equipment, at cost:	
Land	
Buildings and leasehold improvements	

Machinery and equipment	
Total Property, Plant, and Equipment	
Less-Accumulated depreciation and amortization	
Property, Plant, and Equipment-net	
Other Assets:	
Goodwill and other intangibles	
Other	
Total Other Assets	
Total Assets	**$1**
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current Liabilities:	
Current maturities of long-term debt	
Commercial paper, short-term	
Notes payable	
Accounts payable	
Accrued salaries, commissions, and bonuses	
Current portion of self-insurance reserves	
Accrued taxes payable	
Other accrued liabilities	
Total Current Liabilities	
Long-Term Debt, less current maturities	
Deferred Income Taxes	
Self-Insurance Reserves, less current portion	
Other Long-Term Liabilities	
Stockholders' Equity:	
Series A participating preferred stock, $.05 stated value, 500,000 shares authorized, none issued	
Preferred stock, no par value, 500,000 shares authorized, none issued	
Common stock, $1 par value, 120,000,000 shares authorized, 57,918,978 shares issued	
Paid-in capital	
Retained earnings	1
Accumulated other comprehensive income items	
	1
Less-Treasury stock, at cost (16,866,324 shares at November 30, 2000 and 17,090,414 shares at August 31, 2000)	
Total Stockholders' Equity	
Total Liabilities and Stockholders' Equity	**$1**

The accompanying notes to consolidated financial statements are an integral part of these stateme

NATIONAL SERVICE INDUSTRIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME (Unaudited)
(In thousands, except per-share data)

	THREE MONTHS ENDED NOVEMBER 30	
	2000	1999
Sales and Service Revenues:		
Net sales of products	$562,652	$542,294
Service revenues	81,107	77,716
Total Revenues	643,759	620,010
Costs and Expenses:		

Cost of products sold	332,683	323,914
Cost of services	46,433	45,134
Selling and administrative expenses	218,104	196,971
Amortization expense	5,047	5,166
Interest expense, net	13,261	9,986
Other expense (income), net	1,982	(1,013)
Total Costs and Expenses	617,510	580,158
Income before Provision for Income Taxes	26,249	39,852
Provision for Income Taxes	9,712	15,462
Net Income	**$ 16,537**	**$ 24,390**
Per Share:		
Basic Earnings per Share	**$ .40**	**$ .60**
Basic Weighted Average Number of Shares Outstanding	**40,941**	**40,584**
Diluted Earnings per Share	**$ .40**	**$ .60**
Diluted Weighted Average Number of Shares Outstanding	**40,958**	**40,686**

The accompanying notes to consolidated financial statements are an integral part of these stateme

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NATIONAL SERVICE INDUSTRIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)
(In thousands)

Cash Provided by (Used for) Operating Activities
- Net income
- Adjustments to reconcile net income to net cash provided by (used for) operating activities:
  - Depreciation and amortization
  - Provision for losses on accounts receivable
  - (Gain) loss on the sale of property, plant, and equipment
  - Gain on the sale of business
  - Change in assets and liabilities net of effect of acquisitions and divestitures-
    - Receivables
    - Inventories and linens in service, net
    - Deferred income taxes
    - Prepayments and other
    - Accounts payable and accrued liabilities
    - Self-insurance reserves and other long-term liabilities
      - Net Cash Provided by Operating Activities

Cash Provided by (Used for) Investing Activities
- Purchases of property, plant, and equipment
- Sale of property, plant, and equipment
- Acquisitions
- Change in other assets
  - Net Cash Used for Investing Activities

Cash Provided by (Used for) Financing Activities
- Borrowings (repayments) of notes payable, net
- Issuances (repayments) of commercial paper, net (less than 90 days)
- Issuances of commercial paper (greater than 90 days)
- Repayments of commercial paper (greater than 90 days)

Repayments of long-term debt
Treasury stock transactions, net
Cash dividends paid
Net Cash Provided by (Used for) Financing Activities

Effect of Exchange Rate Changes on Cash

Net Change in Cash and Cash Equivalents

Cash and Cash Equivalents at Beginning of Period

Cash and Cash Equivalents at End of Period

Supplemental Cash Flow Information:
Income taxes paid during the period
Interest paid during the period

Noncash Investing and Financing Activities:
Treasury shares issued under long-term incentive plan
Noncash aspects of acquisitions--
Assets acquired
Liabilities assumed or incurred

The accompanying notes to consolidated financial statements are an integral part of these stateme

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NATIONAL SERVICE INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
(Dollar amounts in thousands, except share and per-share data and as

1. BASIS OF PRESENTATION

The interim consolidated financial statements included herein have been prepared by the company without audit and the condensed consolidated balance sheet as of August 31, 2000 has been derived from audited statements. These statements reflect all adjustments, all of which are of a noraml, recurring nature, which are, in the opinion of management, necessary to present fairly the consolidated financial position as of November 30, 2000, the consolidated results of operations for the three months ended November 30, 2000 and 1999, and the consolidated cash flows for the three months ended November 30, 2000 and 1999. Certain reclassifications have been made to the prior year's financial statements to conform to the current year's presentation. Certain information and footnote discolsures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. The company believes that the disclosures are adequate to make the information presented not misleading. It is suggested that these financial statements be read in conjunction with the financial statements and notes thereto inclulded in the company's Annual Report on Form 10-K for the fiscal year ended August 31, 2000.

The results of operations for the three months ended November 30, 2000 are not necessarily indicative of the results to be expected for the full fiscal year because the company's revenues and income are generally higher in the second half of its fiscal year and because of the uncertainty of general business conditions.

2. RECENT ACCOUNTING STANDARDS

Newly Adopted Accounting Standards

Statement of Financial Accounting Standards ("SFAS") No. 133 (as amended by SFAS No. 138), "Accounting for Derivative Instruments and Hedging Activities," was issued in June of 1998 and is effective for all fiscal quarters of fiscal years beginning after June 15, 2000. Accordingly, the company adopted SFAS 133 at the beginning of the quarter ended November 30, 2000. The adoption of this statement did not have a material impact on the company s consolidated financial statements.

Accounting Standards Yet to be Adopted

In September 2000, the Emerging Issues Task Force ("EITF") reached a final consensus on EITF Issue 00-10, "Accounting for Shipping and Handling Fees and Costs." Specifically, Issue 00-10 addresses how the seller of goods should classify amounts billed to a customer for shipping and handling. The EITF concluded that all amounts billed to a customer in a sales transaction related to shipping and handling represent revenues earned for the goods provided and should be classified as revenue. The company is required to and will adopt EITF 00-10 in the fourth quarter of fiscal year 2001. The company has historically netted certain shipping and handling revenues charged to customers in cost and expenses. The adoption of EITF 00-10 will result in an increase in sales and service revenues and cost and expenses, with no impact on net income. The company has not calculated the effect of this reclassification on its reported revenues and costs.

3. BUSINESS SEGMENT INFORMATION

	Sales and Service Revenues	**Operating Profit (Loss)**	**Depreciation and Amortization Expense**	**E A**
Three Months Ended November 30, 2000				
Lighting Equipment	$377,680	$33,276	$12,583	
Chemical	126,355	6,537	2,847	
Textile Rental	81,107	3,727	4,147	
Envelope	58,617	1,712	2,325	
	643,759	45,252	21,902	
Corporate		(5,742)	600	
Interest expense, net		(13,261)		
Total	**$643,759**	**$26,249**	**$22,502**	

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	Sales and Service Revenues	**Operating Profit (Loss)**	**Depreciation and Amortization Expense**	**E A**
Three Months Ended November 30, 1999				
Lighting Equipment	$367,595	$35,287	$12,406	
Chemical	119,901	8,622	2,712	
Textile Rental	77,716	5,128	3,752	
Envelope	54,798	3,068	1,781	
	620,010	52,105	20,651	
Corporate		(2,267)	559	
Interest expense, net		(9,986)		
Total	**$620,010**	**$39,852**	**$21,210**	

	Total Assets November 30, 2000	August 31, 2000
Lighting Equipment	$1,133,007	$1,145,927
Chemical	232,861	241,645

Textile Rental	220,850	222,957
Envelope	153,868	151,003
Subtotal	1,740,586	1,761,532
Corporate	62,371	58,607
Total	**$1,802,957**	**$1,820,139**

4. INVENTORIES

Major classes of inventory as of November 30, 2000 and August 31, 2000 were as follows:

	November 30, 2000	August 31, 2000
Raw Materials and Supplies	$101,376	$104,566
Work-in-Process	19,183	20,262
Finished Goods	150,284	132,751
Total	**$270,843**	**$257,579**

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5. EARNINGS PER SHARE

The company accounts for earnings per share using Statement of Financial Accounting Standards No. 128, "Earnings per Share." Under this statement, basic earnings per share is computed by dividing net earnings available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed similarly but reflects the potential dilution that would occur if dilutive options were exercised. The following table calculates basic earnings per common share and diluted earnings per common share at November 30:

	Three Months Ended November 30	
	2000	19
Basic earnings per common share:		
Net income	$16,537	$24
Basic weighted average shares outstanding (in thousands)	40,941	40
Basic earnings per common share	$ .40	$
Diluted earnings per common share:		
Net income	$16,537	$24
Basic weighted average shares outstanding (in thousands)	40,941	40
Add - Shares of common stock issuable upon assumed exercise of dilutive stock options (in thousands)	17	
Diluted weighted average shares outstanding (in thousands)	40,958	40
Diluted earnings per common share	**$ .40**	**$**

6. COMPREHENSIVE INCOME

The company adopted Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income," in the first quarter of fiscal 1999. SFAS No. 130 requires the reporting of a measure of all changes in equity of an entity that result from recognized transactions and other economic events other than transactions with owners in their capacity as owners. Other comprehensive income (loss) for the three months ended November 30, 2000 and 1999 includes only foreign currency translation adjustments. The calculation of comprehensive income is as follows:

	Three Months Ended November 30	
	2000	1999
Net income	$16,537	$24,390
Other comprehensive income (loss)	(2,518)	(10)
Comprehensive Income	**$14,019**	**$24,380**

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7. LEGAL PROCEEDINGS

The company is subject to various legal claims arising in the normal course of business out of the conduct of its current and prior businesses, including patent infringement and product liability claims. Based on information currently available, it is the opinion of management that the ultimate resolution of pending and threatened legal proceedings will not have a material adverse effect on the company's financial condition or results of operations. However, in the event of unexpected future developments, it is possible that the ultimate resolution of such matters, if unfavorable, could have a material adverse effect on the company's results of operations in a particular future period. The company reserves for known legal claims when payments associated with the claims become probable and the costs can be reasonably estimated. The actual costs of resolving legal claims may be substantially lower or higher than that reserved. The company does not believe that the amount of such costs below or in excess of that reserved is reasonably estimable.

Among the product liability claims to which the company is subject are claims arising from the installation and distribution of asbestos-containing insulation, primarily in the southeastern United States, by a previously divested business of the company. The company has reached settlement agreements with substantially all of its relevant insurers providing for their payment of these claims up to the various policy limits. Over the past two decades, through November 30, 2000, approximately 35,800 such claims against the company's business have been resolved for an aggregate cost (liability payments and other expenses) of approximately $40 million, approximately $39 million of which has been paid by insurers. The average per-claim liability payment made by the company and its insurers is less than nine hundred dollars over that period and is slightly more than a thousand dollars over the past two years. As of November 30, 2000, there were approximately 31,400 similar claims pending against the company, including approximately 16,000 claims that have been settled in principle (but not yet finalized) for amounts generally consistent with recent historical per-claim settlement costs. The company anticipates that similar claims will be made in the future. Neither the number of such claims nor the liabilities which may arise from them is reasonably estimable.

Since 1988 the company has been a member, together with a number of other companies that are among the defendants in these claims, of the Center for Claims Resolution (the "CCR"), which has handled all such claims on behalf of the company. The company has been responsible for varying percentages of CCR's defense and liability payments on a claim-by-claim basis pursuant to predetermined sharing formulae; substantially all of the company's portion of those payments have been paid directly by the company's insurers. During 2000, one member left the CCR; another member had its membership terminated by the CCR's Board; and another member declared bankruptcy. These members have failed to pay certain financial obligations in connection with settlements that were reached while they were CCR members. The company expects to pay CCR approximately five hundred thousand dollars for the company's allocated share of the amount needed to cover defaulted obligations relating to paid settlements; the CCR may request, and the company may be subject to claims that it has liability for, further payments with respect to settlements reached in principle but not finalized. Although the company would seek to recover any such payments from insurance and other sources, there is no assurance that such payments, if made by the company, would be recoverable. In addition, several significant companies that are traditional co-defendants in similar claims but are not members of CCR sought bankruptcy protection during 2000. The absence of these traditional defendants may increase the cost of resolving similar claims for other defendants, including the company and the other remaining CCR members. The company expects that beginning on or about February 1, 2001, it will use CCR for claims processing and handling but not for sharing of liability costs; the company will also use coordinating counsel and will participate more directly in defense of claims.

The ultimate asbestos-related liability of the company is difficult to estimate. Based on the company's experience to date, the company believes that substantially all of the costs it may incur in defending and ultimately disposing of asbestos-related claims will be paid by its insurers. The company is and will continue monitoring and analyzing the trends, developments, and variables affecting or likely to affect the resolution of pending and future claims against the company.

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8. ENVIRONMENTAL MATTERS

The company's operations, as well as similar operations of other companies, are subject to comprehensive laws and regulations relating to the generation, storage, handling, transportation, and disposal of hazardous substances and solid and hazardous wastes and to the remediation of contaminated sites. Permits and environmental controls are required for certain of the company's operations to limit air and water pollution, and these permits are subject to modification, renewal, and revocation by issuing authorities. The company believes that it is in substantial compliance with all material environmental laws, regulations, and permits. On an ongoing basis, the company incurs capital and operating costs relating to environmental compliance. Environmental laws and regulations have generally become stricter in recent years, and the cost of responding to future changes may be substantial.

The company's environmental reserves, which are included in current liabilities, totaled $10.1 million and $10.2 million at November 30 and August 31, 2000, respectively. The actual cost of environmental issues may be substantially lower or higher than that reserved due to the difficulty in estimating such costs, potential changes in the status of government regulations, and the inability to determine the extent to which contributions will be available from other parties. The company does not believe that any amount of such costs below or in excess of that accrued is reasonably estimable.

Certain environmental laws, such as Superfund, can impose liability for the entire cost of site remediation upon each of the current or former owners or operators of a site or parties who sent waste to a site where a release of a hazardous substance has occurred regardless of fault or the lawfulness of the original disposal activity. Generally, where there are a number of potentially responsible parties ("PRPs") that are financially viable, liability has been apportioned based on the type and amount of waste disposed of by each party at such disposal site and the number of financially viable PRPs, although no assurance as to the method of apportioning the liability can be given as to any particular site.

The company is currently a party to, or otherwise involved in, legal proceedings in connection with state and federal Superfund sites, two of which are located on property owned by the company. Except for the Crymes Landfill and M&J Solvents matters in Georgia, the company believes its liability is de minimis at each of the sites which it does not own where it has been named as a PRP. At the Crymes Landfill and M&J Solvents sites in Georgia, since the matters are currently in the investigative phase, the company does not know whether its liability is de minimis but believes that its exposure at each of the sites is not likely to result in a material adverse effect on the company due to its limited involvement at the sites and the number of viable PRPs. For property which the company owns on Seaboard Industrial Boulevard in Atlanta, Georgia, the company has conducted an investigation on its and adjoining properties and submitted a Compliance Status Report ("CSR") to the State of Georgia Environmental Protection Division ("EPD") pursuant to the Georgia Hazardous Site Response Act. The CSR is subject to EPD's final approval. Until the CSR is finalized, the company will not be able to determine if remediation will be required, if the company will be solely responsible for the cost of such remediation, or whether such cost is likely to result in a material adverse effect on the company. For property which the company owns on East Paris Street in Tampa, Florida, the company has been requested by the State of Florida to clean up chlorinated solvent contamination in the groundwater on the property and on surrounding property known as Seminole Heights Solvent Site and to reimburse approximately $430 thousand of costs already incurred by the State of Florida in connection with such contamination. The company believes that it has a strong defense due to likely off-site sources of the contamination and because contamination from the property, if any, was due to prior owners and not the company's operations. At this time, it is too early to quantify the company's potential exposure or the likelihood of an adverse result.

In connection with the sale of the North Bros. business and 29 of the company's textile rental plants in 1997, the company has retained environmental liabilities arising from events occurring prior to the closing, subject to certain exceptions. The company has received notice from the buyer of the textile rental plants of the alleged presence of perchloroethylene contamination on one of the properties involved in the sale. The company has since asserted an indemnification claim against the company from which it bought the property. The prior owner is currently conducting an investigation of the contamination at its expense, subject to a reservation of rights. At this time, it is too early to quantify the company's potential exposure in this matter, the likelihood of an adverse result, or the possibility that the company may be fully or partially indemnified.

The State of New York has filed a lawsuit against the company alleging that the company is responsible as a successor to Serv-All Uniform Rental Corp. for past and future response costs in connection with the release or potential release of hazardous substances at and from the Blydenburgh Landfill in Islip, New York. The company believes that it is not a successor to Serv-All Uniform Rental Corp. and therefore has no liability with respect to the Blydenburgh Landfill, and it has responded to the lawsuit accordingly. At this stage of the litigation, it is too early to quantify the company's potential exposure or the likelihood of an adverse result.

MANAGEMENT'S DISCUSSION AND ANALYSIS

OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with the consolidated financial statements and related notes.

National Service Industries is a diversified service and manufacturing company operating in four segments: lighting equipment, chemicals, textile rental, and envelopes. The company remained in solid financial condition at November 30, 2000. Net working capital was $234.0 million, up from $221.1 million at August 31, 2000, and the current ratio remained constant at 1.4. At November 30, 2000, the company's percentage of debt to total capitalization increased slightly to 49.1 percent compared to 49.0 percent at August 31, 2000.

Results of Operations

National Service Industries generated revenue of $643.8 million in the three months ended November 30, 2000, compared to revenue of $620.0 million in the previous year. The increase was related to growth in the company's core businesses, primarily in the lighting equipment and chemical segments.

Net income totaled $16.5 million, or $.40 per diluted share, for the three months ended November 30, 2000, compared to net income of $24.4 million, or $.60 per diluted share, for the three months ended November 30, 1999. Net income declined $7.9 million primarily because of increased interest expense and costs incurred to reposition the business for an anticipated economic slowdown. Interest expense increased $3.3 million as a result of higher interest rates and increased debt levels associated with working capital increases. Additional costs to reposition the businesses were associated with the closing and streamlining of operations and the rollout of technological enhancements. Management expects these initiatives to reduce the company's cost structure and improve service capability. Anticipated higher interest costs and continued investments to improve the company's cost structure are forecasted to negatively impact second quarter performance, with first half results as much as thirty percent lower than last year's first half results. However, management expects reductions in the company's cost structure to contribute to improved second half results.

The lighting equipment segment reported revenue of $377.7 million for the first quarter, an increase of $10.1 million over the previous year. The increase in revenue resulted primarily from higher sales volumes in its core business. However, a recent slowing of order rates may indicate an initial weakening in the non-residential construction market. Excluding a $1.0 million pretax charge during the first quarter of fiscal 2000 for closing a manufacturing facility in California, operating profit decreased approximately $3.0 million, from $35.3 million to $33.3 million, because of planned promotional costs associated with home center retail sales, increased spending for information technology, and costs to establish a Texas distribution center.

In the chemical segment, revenue increased $6.5 million, or 5.4 percent, due to sales volume growth in its core business. Operating profit of $6.5 million was $2.1 million lower than last year's results primarily because of costs incurred in conjunction with the consolidation of the Zep and Selig manufacturing operations and costs associated with a North American direct sales force training meeting. Management expects to benefit from these initiatives during the second half of the fiscal year through reduced operating costs and through improved direct sales force effectiveness.

The textile rental segment generated revenue of $81.1 million during the first quarter, representing a 4.4 percent increase over last year. This increase was attributable primarily to revenues associated with acquired businesses. Operating profit was $3.7 million compared to $5.1 million a year ago. The decline in operating profit was primarily related to costs incurred to close a facility in order to reduce the segment's cost structure and improve customer service.

Envelope segment revenue increased 7.0 percent from $54.8 million to $58.6 million. The increase was primarily due to higher sales volumes to strategic partners. Operating profit decreased $1.4 million to $1.7 million primarily because of costs associated with reorganizing the Miami, Florida manufacturing facility.

Corporate expenses totaled $5.7 million, compared to $2.3 million one year ago, primarily as a result of lower-than-normal prior-year long-term incentive compensation expense. Additionally, the provision for income taxes decreased to 37.0 percent of pretax income for the first quarter compared to 38.8 percent in the prior year, primarily due to the implementation of various tax-saving strategies impacting fiscal 2001.

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Liquidity and Capital Resources

Operating Activities

Operations provided cash of $19.0 million during the first quarter of fiscal 2001 compared with $29.7 million during the respective period of the prior year. Fiscal 2001 operating cash flow was lower primarily because of a decrease in net income.

Investing Activities

Investing activities used cash of $11.9 million versus $34.3 million in the prior year. The improvement in investing cash flows related primarily to a decrease in acquisition spending and a decrease in purchases of property, plant, and equipment. Higher acquisition spending in fiscal 2000 was primarily due to remaining payments associated with the 1999 acquisition of Holophane.

Capital expenditures totaled $14.7 million compared to $21.8 million in the first quarter of last year. In the first quarter of fiscal 2001, the lighting equipment segment invested primarily in manufacturing upgrades and improvements. Capital expenditures in the envelope segment were primarily related to manufacturing process improvements and information systems. In the chemical segment, capital expenditures were associated with manufacturing equipment and facilities improvements. Capital investments in the textile rental segment were mainly attributable to building improvements, replacing old equipment, and information systems. In the first quarter of fiscal 2000, the lighting equipment segment invested in land, buildings, and equipment for a new plant in Mexico and in manufacturing upgrades and improvements. Capital expenditures in the envelope segment related primarily to new folding capacity. The textile rental segment's expenditures related to replacing old equipment and delivery truck refurbishments. Management believes current cash balances, anticipated cash flows from operations, available funds from the commercial paper program or the committed credit facilities, and the complimentary lines of credit are sufficient to meet the company's planned level of capital spending and general operating cash requirements for the next twelve months.

Financing Activities

Cash used by financing activities totaled $5.4 million in the current-year first quarter compared to cash provided of $3.9 million in fiscal 2000 primarily as a result of a decrease in cash provided by net borrowings. First quarter dividend payments totaled $13.5 million, or 33 cents per share, compared with $13.0 million, or 32 cents per share, for the prior-year period.

Legal Proceedings

For information concerning legal proceedings, including trends and developments involving legal proceedings, see footnote 7 to the financial statements included in this filing.

Environmental Matters

For information concerning environmental matters, see footnote 8 to the financial statements included in this filing.

Quantitative and Qualitative Disclosures About Market Risk

The company is exposed to market risks that may impact the Consolidated Balance Sheets, Consolidated Statements of Income, and Consolidated Statements of Cash Flows due to changing interest rates and foreign exchange rates. The company does not currently participate in any significant hedging activities, nor does it currently utilize any derivative financial instruments. The following discussion provides additional information regarding the company's market risks.

Interest Rates- Interest rate fluctuations expose the company's variable-rate debt to changes in interest expense and cash flows. The company's variable-rate debt, primarily commercial paper, amounted to $286.8 million at November 30, 2000. Based on outstanding borrowings at quarter end, a 10 percent adverse change in effective market interest rates at November 30, 2000 would result in additional annual after-tax interest expense of approximately $1.2 million. Although a fluctuation in interest rates would not affect interest expense or cash flows related to the $160 million and $200 million publicly traded notes, the company's primary fixed-rate debt, a 10 percent increase in effective market interest rates at November 30, 2000 would decrease the fair value of these notes to approximately $134 and $193 million, respectively.

Foreign Exchange Rates-The majority of the company's revenue, expense, and capital purchases are transacted in U.S. dollars. International operations during the first quarter of fiscal 2001, primarily in the lighting equipment and chemical segments, represented less than 10 percent of revenue, operating profit, and long-lived assets. The company does not believe a 10 percent fluctuation in average foreign currency rates would have a material effect on its consolidated financial statements or results of operations.

Cautionary Statement Regarding Forward-Looking Information

This filing contains forward-looking statements, within the meaning of the Private Securities Litigation Reform Act of 1995, that involve risks and uncertainties. Consequently, actual results may differ materially from those indicated by the forward-looking statements. Statements made herein that may be considered forward looking include statements concerning: (a) anticipated future benefits of initiatives undertaken to reduce the company's cost structure and improve the company's service capability; (b) anticipated higher interest costs and investments to improve the company's cost structure and their impact on second quarter performance; (c) expected earnings during the first half, second half, and full fiscal year of 2001; (d) indications of a weakening in the non-residential construction market; and (e) the realization of expected benefits through reduced operating costs and improved direct sales force effectiveness in the chemical segment during the second half of the fiscal year. A variety of risks and uncertainties could cause the company's actual results to differ materially from the anticipated results or other expectations expressed in the company's forward-looking statements. The risks and uncertainties include without limitation the following: (a) the uncertainty of general business and economic conditions, including the potential for a greater-than-expected slowdown in non-residential construction awards, interest rate changes, and fluctuations in commodity and raw material prices; (b) unexpected developments and outcomes in the company's legal and environmental proceedings; (c) the company's ability to realize the anticipated benefits of strategic initiatives related to increased productivity, new product development, technological advances, cost synergies, decreases in net working capital, and the achievement of sales growth across the business segments; and (d) the successful completion of changes to manufacturing operations.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

For information concerning legal proceedings, including trends and developments involving legal proceedings, see footnote 7 to the financial statements included in this filing.

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

At the annual meeting of stockholders held December 21, 2000, all nominees for director were elected to the board without opposition and Arthur Andersen LLP's appointment as independent auditor for the current fiscal year was ratified. The elected board members are as follows:

James S. Balloun, Chairman	David Levy	Betty L
Leslie M. Baker, Jr.	Sam Nunn	Kathy B
John L. Clendenin	Roy Richards, Jr.	Barrie
Thomas C. Gallagher	Ray M. Robinson	Neil Wi

In addition, stockholders voted on the following:

		Votes Cast
	Affirmative	Negative
Stockholder proposal recommending the sale of the Corporation	2,239,287	21,932,10

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits are listed on the Index to Exhibits (page 15).

(b) There were no reports on Form 8-K for the three months ended November 30, 2000.

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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.

NATIONAL SERVICE INDUSTRIES, INC.

REGISTRANT

DATE January 9, 2001

/S/ KENYON
KENYON MUR
SENIOR VIC
GENERAL CO

DATE January 9, 2001

/S/ BROCK
BROCK HATT
EXECUTIVE
CHIEF FINA

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INDEX TO EXHIBITS

EXHIBIT 10(iii)A (1) Incentive Stock Option Agreement for Executive Officers Effec

Beginning October 24, 2000 between National Service Industrie
and Joseph G. Parham, Jr.

(2) Nonqualified Stock Option Agreement for Executive Officers Ef
Beginning October 4, 2000 between National Service Industries
and:

(a) James S. Balloun
(b) Brock A. Hattox
(c) David Levy

(3) Nonqualified Stock Option Agreement for Executive Officers Ef
Beginning October 24, 2000 between National Service Industrie
and:

(a) James S. Balloun
(b) George H. Gilmore
(c) Brock A. Hattox
(d) David Levy
(e) Joseph G. Parham, Jr.

(4) Restricted Stock Award Agreement Effective Beginning October
between National Service Industries, Inc. and:

(a) James S. Balloun
(b) George H. Gilmore
(c) Brock A. Hattox
(d) David Levy
(e) Joseph G. Parham, Jr.