MEXICAN RESTAURANTS INC
Form 10-Q
May 15, 2001

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UNITED STATES

SECURITIES & 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 April 1, 2001

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: 0-28234

MEXICAN RESTAURANTS, INC.
(Exact name of registrant as specified in its charter)

TEXAS	76-0493269
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification Number)
1135 EDGEBROOK, HOUSTON, TEXAS	77034-1899
(Address of Principal Executive Offices)	(Zip Code)

Registrant's telephone number, including area code: 713-943-7574

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 [ ]

Number of shares outstanding of each of the issuer's classes of common stock, as of May 11, 2001: 3,522,905 shares of common stock, par value $.01.

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PART 1 - FINANCIAL INFORMATION

Item 1. Financial Statements

Mexican Restaurants, Inc. and Subsidiaries

Consolidated Balance Sheets

ASSETS	4/1/01	
Current assets:		
Cash and cash equivalents	$ 1,116,230	$
Royalties receivable	69,342	
Other receivables	673,518	
Inventory	591,219	
Taxes receivable	90,283	
Prepaid expenses and other current assets	704,914	
Total current assets	3,245,506	
Property, plant and equipment	25,639,040	
Less accumulated depreciation	(7,661,554)	
Net property, plant and equipment	17,977,486	
Deferred tax assets	1,108,456	
Property held for resale	1,100,000	
Other assets	8,376,181	
	$ 31,807,629	$
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Current installments of long-term debt	$ --	$
Accounts payable	2,285,918	
Accrued sales and liquor taxes	495,665	
Accrued payroll and taxes	1,198,397	
Accrued expenses	906,764	
Total current liabilities	4,886,744	
Long-term debt, net of current portion	8,100,000	
Other liabilities	584,654	
Deferred gain	2,981,975	
Stockholders' equity:		
Preferred stock, $.01 par value, 1,000,000 shares authorized	--	
Capital stock, $0.01 par value, 20,000,000 shares authorized, 4,732,705 shares issued	47,327	
Additional paid-in capital	20,121,076	
Retained earnings	6,409,764	
Deferred compensation	(161,193)	
Treasury stock, cost of 1,191,000 and 1,135,000 shares, respectively	(11,162,718)	(
Total stockholders' equity	15,254,256	
	$ 31,807,629	$

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MEXICAN RESTAURANTS, INC. AND SUBSIDIARIES

Consolidated Statements of Income

	13-WEEK PERIOD ENDED 04/01/01	13-WEEK PERIOD ENDED 4/02/00
Revenues:		
Restaurant sales	$ 15,451,021	$ 15,545,467
Franchise fees and royalties	306,491	341,839
Other	20,489	5,402
	15,778,001	15,892,708
Costs and expenses:		
Cost of sales	4,249,537	4,410,447
Labor	5,111,579	5,214,059
Restaurant operating expenses	3,784,719	3,556,370
General and administrative	1,295,250	1,374,593
Depreciation and amortization	573,593	496,000
Pre-opening costs	254	50,901
Asset impairments and restaurant closing costs	--	--
	15,014,932	15,102,370
Operating income (loss)	763,069	790,338
Other income (expense):		
Interest income	10,674	4,416
Interest expense	(191,752)	(204,898)
Other, net	9,768	(1,271)
	(171,310)	(201,753)
Income before income tax expense	591,759	588,585
Income tax expense	207,116	206,000
Net income	$ 384,643	$ 382,585
Basic and diluted income per share	$ 0.11	$ 0.11
Weighted average number of shares (basic and diluted)	3,526,107	3,620,914
	3,530,718	3,620,953

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MEXICAN RESTAURANTS, INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows

(unaudited)

	13-WEEK PERIODS ENDED 4/1/01	4/2/00
Cash flows from operating activities:		
Net income	$ 384,643	$ 382,58
Adjustments to reconcile net income to net cash provided by operating activities:		
Deferred compensation	10,326	12,83
Depreciation and amortization	573,593	496,00
Deferred gain amortization	(60,857)	(63,52
Deferred taxes	59,205	-
Loss on sale of fixed assets	1,368	9,67
Changes in assets and liabilities:		
Royalties receivable	(2,544)	(51,11
Other receivables	(61,915)	(55,93
Income tax receivable/payable	166,797	80,30
Inventory	127,410	10,70
Prepaid and other current assets	(182,010)	(48,81
Other assets	(9,886)	24,32
Accounts payable	(667,731)	(847,58
Accrued expenses and other liabilities	814,362	165,12
Other liabilities	49,150	51,13
Total adjustments	817,268	(216,87
Net cash provided by operating activities	1,201,911	165,70
Cash flows from investing activities:		
Payment for purchase of acquisition, net of cash acquired	--	-
Purchase of property, plant and equipment	(492,640)	(830,79
Proceeds from sale of property, plant and equipment	--	176,39
Net cash used in investing activities	(492,640)	(654,39
Cash flows from financing activities:		
Net borrowings under line of credit	(200,000)	160,00
Purchase of treasury stock	(29,375)	-
Net cash provided by (used in) financing activities	(229,375)	160,00
Increase (decrease) in cash and cash equivalents	479,896	(328,68
Cash and cash equivalents at beginning of period	636,334	743,93
Cash and cash equivalents at end of period	$ 1,116,230	$ 415,24
Supplemental disclosure of cash flow information:		
Cash paid during the period:		
Interest	$ 93,161	$ 345,65
Income Taxes	$ 7,375	$ 679,46
Non-cash investing and financing activity:		
Sale of property for note receivable	$ 244,109	$ -

MEXICAN RESTAURANTS, INC. AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

In the opinion of Mexican Restaurants, Inc. (the "Company"), the accompanying consolidated financial statements contain all adjustments (consisting only of normal recurring accruals and adjustments) necessary for a fair presentation of the consolidated financial position as of April 1, 2001, and the consolidated statements of income and cash flows for the 13-week periods ended April 1, 2001 and April 2, 2000. The consolidated statements of income for the 13-week period ended April 1, 2001 is not necessarily indicative of the results to be expected for the full year.

2. Accounting Policies

During the interim periods the Company follows the accounting policies set forth in its consolidated financial statements in its Annual Report and Form 10-K (file number 0-28234). Reference should be made to such financial statements for information on such accounting policies and further financial details.

3 Net Income (loss) per Common Share

Basic income per share is based on the weighted average shares outstanding without any dilutive effects considered. Diluted income per share reflects dilution from all contingently issuable shares, including options and warrants. Stock options and warrants outstanding at April 1, 2001 and April 2, 2000 of 949,570 and 725,270 shares, respectively, were not considered in the computation of net income per common share because the effect of their inclusion would have been antidilutive.

Item 2 Management's Discussion And Analysis Of Financial Condition And Results Of Operations

Special Note Regarding Forward-Looking Statements

This Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such factors include, among others, the following: accelerating growth strategy; dependence on executive officers; geographic concentration; increasing susceptibility to adverse conditions in the region; changes in consumer tastes and eating habits; national, regional or local economic and real estate conditions; demographic trends; inclement weather; traffic patterns; the type, number and location of competing restaurants; inflation; increased food, labor and benefit costs; the availability of experienced management and hourly employees; seasonality and the timing of new restaurant openings; changes in governmental regulations; dram shop exposure; and other factors not yet experienced by the Company. The use of words such as "believes", "anticipates", "expects", "intends" and similar expressions are intended to identify forward-looking statements, but are not the exclusive means of identifying such statements. Readers are urged to carefully review and consider the various disclosures made by the Company in this report and in the Company's Annual Report and Form 10-K for the fiscal year ended December 31, 2000, that attempt to advise interested parties of the risks and factors that may affect the Company's business.

Results of Operations

Revenues. The Company's revenues for the first quarter of fiscal 2001 were down $114,707 or 0.7% to $15.8 million compared with the same quarter a year ago. Restaurant sales for the first quarter of 2001 were down $94,446 compared with the same quarter a year ago, to $15.5 million. The decline was due to a decrease in the number of restaurants. Two restaurants were closed, one was converted to a franchise and one new restaurant was opened since the end of the first quarter of fiscal 2000. Company-owned same-store sales for the quarter increased 2.8%. Franchise-owned same-stores sales for the quarter increased 2.1%.

Costs and Expenses. Cost of sales, consisting primarily of food and beverage costs, but also including paper and supplies, decreased as a percentage of restaurant sales in the first quarter of 2001 to 27.5% as compared with 28.4% in the same quarter in fiscal 2000. The improvement was primarily due to a menu price increase across all concepts, except Casa Ole. This was partly offset by small increases in meat and cheese prices.

Labor and other related expenses decreased as a percentage of restaurant sales to 33.1% in the first quarter of 2001 as compared with 33.5% in the same quarter in fiscal year 2000. The decrease was primarily due to operating improvements at the Tortuga Coastal Cantina restaurants. The improvement was also partly due to last year's closure of under performing restaurants. Offsetting these improvements were workers' compensation insurance increases of 120.0%.

Restaurant operating expenses, which primarily includes rent, property taxes, utilities, repair and maintenance, liquor taxes and advertising, increased as a percentage of restaurant sales to 24.5% in the first quarter of 2001 as compared with 22.9% in the same quarter in fiscal 2000. The majority of the increase was due to higher utility costs.

General and administrative expenses decreased by 5.8%, or $79,343 from the same quarter in fiscal 2000. The decrease was due primarily to staff reductions in January 2001, resulting in a decrease in compensation costs. General and administrative expenses were 8.2% of total revenues in the first quarter of fiscal 2001 compared to 8.6% in the first quarter of fiscal 2000.

Depreciation and amortization expense of $573,593, increased by $77,393 compared to the same quarter in the last fiscal year. This was due to the addition of two new stores in February and October 2000, four remodelings during fiscal 2000, as well as other fixed asset additions in the last four quarters. The closed restaurants mentioned above had relatively low book values of fixed assets so their closure did not significantly reduce depreciation.

Pre-opening costs decreased approximately $50,000 as no new restaurants were opened in the first quarter of 2001. One new restaurant was opened in the first quarter of fiscal 2000.

Other Income (Expense). Net other income (expense) of $171,310 decreased by $30,443 compared to the same quarter in the last fiscal year. The decrease was due primarily to a decreased level of debt and a reduction in interest rates. The average debt balance was 9.1% lower than the balance in the comparable quarter last year.

Income Tax Expense. The Company's effective tax rate was 35.0% in both the 1st quarter of 2001 and the comparable quarter last year. Expense changed by less than $1,200.

Liquidity and Capital Resources

Net cash provided by operating activities was $1.2 million for the 13-week period ended April 1, 2001, compared to $0.2 million for the same period last year. As of April 1, 2001, the Company had a working capital deficit of $1.6 million, which is common in the restaurant industry, since restaurant companies do not typically require a significant investment in either accounts receivable or inventory.

During the first 13 weeks of 2001, capital expenditures on property, plant and equipment were approximately $0.5 million as compared to $0.8 million for the same period in 2000. Capital expenditures included the remodeling of two restaurants. Additionally, the Company had cash outlays for necessary replacement of equipment and leasehold improvements in various older units. The Company estimates its capital expenditures for the remainder of the fiscal year will be approximately $1.1 million.

The Company has a $9.5 million credit facility with Bank of America. At December 31, 2001, the credit facility will be reduced to $8.5 million and will mature on July 15, 2002. The interest rate is either the prime rate or LIBOR plus a stipulated percentage. Accordingly, the Company is impacted by changes in the prime rate and LIBOR. The Company is subject to a non-use fee ranging from 0.25% to 0.5% on the unused portion of the revolver from the date of the credit agreement. As of April 1, 2000, the Company had $8.1 million outstanding on the revolving line of credit. The acquisition of La Senorita, which closed on April 30, 1999, used $4.2 million of the revolving line. The balance was used for new restaurant construction, remodeling and other working capital needs.

Bank of America notified the Company in early February 2001 that it was asking the Company to find a replacement lender. They also indicated that to facilitate the effort they were moving the Company's account to the bank's Special Assets Group. As of December 31, 2000, the Company was in compliance with all of its loan covenants. However, based on tighter covenants that went into effect in the first quarter of fiscal 2001, the Company was out of compliance with a loan covenant at the end of the first quarter of fiscal 2001 and anticipates being out of compliance at the end of the second quarter. The bank, in return for additional fees and an increase in interest rates, has agreed to waive the 2001 first and second quarter lack of compliance and amend certain future covenant ratios under the debt agreement. The Company has received and is evaluating alternative finance proposals from several lenders. The goal is to enter into a term loan for at least $5.0 million, and to establish a new revolving line of credit. Without property sales, the Company anticipates that it will use excess cash flow during fiscal 2001 to pay down approximately $2.0 million of outstanding indebtedness.

The Company also has a $9.8 million forward commitment agreement with Franchise Finance Corporation of America ("FFCA"). At April 1, 2001, the Company had approximately $9.8 million available under the FFCA forward commitments.

The Company's management believes that with its forward commitments with Franchise Finance Corporation of America, along with operating cash flow and the Company's revolving line of credit with Bank of America (and its successor), funds will be sufficient to meet operating requirements and to finance routine capital expenditures and remodels through the end of the 2001 fiscal year.

Recent Accounting Pronouncements

Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities ("SFAS 133"), was issued by the Financial Accounting Standards Board in June 1998. SFAS 133 standardizes the accounting for derivative instruments, including certain derivative instruments embedded in other contracts. Under the standard, entities are required to carry all derivative instruments in the statement of financial position at fair value. The Company adopted SFAS 133 beginning in fiscal year 2001. The Company does not expect the adoption of SFAS 133 to have a material effect on its financial condition or results of operation because the Company does not enter into derivative or other financial instruments for trading or speculative purposes nor does the Company use or intend to use derivative financial instruments or derivative commodity instruments.

Item 3. Quantitative And Qualitative Disclosures About Market Risk

The Company does not have or participate in transactions involving derivative, financial and commodity instruments. The Company's long-term debt bears interest at floating market rates. Based on amount outstanding at April 1, 2001, a 1% change in interest rates would change interest expense by $20,000.

PART II - OTHER INFORMATION

Not Applicable

SIGNATURES

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

Mexican Restaurants, Inc.

Dated: May 15, 2001 By: /s/ Curt Glowacki
Curt Glowacki
Chief Executive Officer
(Principal Executive Officer)

Dated: May 15, 2001 By: /s/ Andrew J. Dennard
Andrew J. Dennard
Vice President, Chief Financial Officer & Treasurer
(Principal Financial Officer and
Principal Accounting Officer)