

ANALYZING THE ANNUAL REPORT --

FREDS INC FRED 2004

Millions of dollars - except today's price

The cheaper the paper, the more valuable the information -- Peter Lynch (Company) (Symbol) (Year of report)

Press Ctrl+D to delete current data. Ctrl+I to insert OPS data. See the bottom of the form for instructions

Accounts Receivable Change: **-3%** OK!, Right direction (Decreasing)

Days waiting for payment this year= **5**

Days waiting for payment prior year= **6**

Below 60 is good - below 45 is superb

Inventories Change: **15%** Whoa, wrong direction (Increasing)

Inventory Turnover Days this year = **97** If Sales is flat or decreasing, Caution

Compare with other companies in the industry If Inventories are rising faster than sales, competition or pricing are likely the problem

Sales or Revenues Change: **11%** Way to GO! (Increasing)

Sales to Accts Receivable Ratio. OK (Sales growing faster than Accts Receivable)

Sales to Inventories Ratio. Caution: Inventories growing faster than sales

Plant & Equipment Change: **7%** OK - (Sales should grow as fast)

(Sales should be increasing as fast or faster). Way to GO! Sales are growing faster

Long-term Debt Change: **283%** Wrong direction (Increasing)

Why are they taking on more debt? What is the debt to equity ratio?

Total Interest Coverage Pretax exceeds interest X times **65** Large numbers aren't as useful as small.

[Pretax Profit + Total Interest Paid / Total Interest Paid]

This company appears to be in good shape financially.

Any number below 5 is worrisome. A number below 3 is very worrisome

Number of shares outstanding trend: Even **1%** No significant change

[Curr. Yr. Shares/Prior Yr. Shares]

A small change of up to about 2% isn't considered too consequential

Cost of Sales Up **11%** Caution - Why is it increasing?

[Cost of sales this year/Cost of sales prior year as a % change]

CAUTION - Cost of Sales increasing faster than Sales

Cashflow Growth **-42%** Cashflow should increase at the same rate as Sales - or greater

[Curr. Yr. Cash from Operations/Prior Yr. Cash from Operations]

Caution - Cashflow is not increasing at or better than the Sales rate

Free Cash Flow Margin **-4%** OOPS, anything less than 10 is bad news

[Free Cash Flow / Sales]

Earnings Confidence Rating -- Measures quality of Earnings **1.38** Generally the closer this is to 1, the higher the quality of Earnings

[Net Income/Net Cash from Operations]

	Net Income	Net Cash
Compare - Net Income with Net Cash	-12%	-42%

Oops - Net Cash is growing at a slower rate than Net Income

Caution - Net Income is declining Caution - Net Cash is declining

CAUTION: Check for accuracy if using OPS data

Cash Position per Share: **-\$0.44** per share in cash beyond debt. A small negative amount isn't considered too serious. But if cash is shrinking and

[Net Cash / Shrs outstanding]

Offers price support in falling market if positive.

debt is growing, company may be in weak financial shape.

LT Debt to Equity Ratio: **7%** debt to equity. Long-term Debt is in normal range

[Long-term Debt / Total Equity]

Normal Long-term Debt -- Less than 25% debt.

NOTE: Ratios are more meaningful if compared to other companies in the same industry.

Quick Ratio: **0.2 to 1** About 1:1 is normal. The higher the better.

[Cash+Markable Securities+Accts Rec. / Total Liabilities]

This is a relatively severe test of a company's liquidity and its ability to meet short-term obligations.

Working Capital Ratio: **2.8 to 1** About 2:1 is normal for manufacturer. 1:1 normal for Utilities.

[Total Current Assets / Total Current Liabilities]

Danger
Caution
Good
Very Good

Inventory Turnover Ratio: **3.8 to 1** The higher the ratio the better. Indicates quality merchandise & proper pricing.

[Cost of Sales / Inventory]

Also note the number of days Inventories are held before they become a product and sold (See "Inventories" above).

Plant Turnover Ratio: **10.4 to 1** The higher the ratio the better. If plant or equipment are added, sales should increase.

(Sales / Prop. Plant & Equip.)

Be aware it takes time for a new plant to come on line and benefit sales. Check to see what the funds for PP&E were spent for.

Price to Sales Ratio: \$ **0.42** The lower the amount the better. This is the amount invested for each dollar of sales. This ratio is Industry sensitive.

[Today's Price / Revenues per Share]

This ratio will be higher for companies with high profit margins and growth. Compare to same industry companies.

1	\$5	Cash (see Balance Sheet)
2	\$0	Marketable Securities or Investments
3	\$19	Accounts Receivable this year
3	\$20	Accounts Receivable prior year
4	\$275	Inventories current year
4	\$240	Inventories prior year
5	\$319	Total Current Assets
6	\$139	This Yr. Total Property Plant & Equip.
6	\$130	Prior Yr. Total Property Plant & Equip.
7	\$115	Total Current Liabilities
8	\$23	Long-term Debt this year
8	\$6	Long-term Debt prior year
9	40	Common Shares Outstanding this Yr.
9	39	Common Shares Outstanding prior Yr.
10	\$315	Total Stockholders Equity
		(see Consolidated Statement of Earnings)
11	\$1,442	Total Sales or Revenues this Year
11	\$1,303	Total Sales or Revenues prior Year
11a	\$1,036	Cost of Sales this Year
11a	\$935	Cost of Sales prior Year
11b	\$38	Income before Taxes
11d	\$29	This Yr. Net Income
11d	\$33	Prior Yr. Net Income
11e	\$1	Total Interest Paid on Debt (from Ann. Rpt)
	64.5	Total Interest Coverage (from OPS)
		(see Statement of Cash Flows)
12	21	This Yr. -Net Cash provided by Operations
12	36	Prior Yr. -Net Cash provided by Operations
14	\$35	Acquisition of Property Plant & Equipment
13	\$3	Total Dividends paid (if any)
	\$15.09	Today's Price per Share
	jun 6 2005	Date of Price quote

Web site - http://www.homestead.com/bobadams/bobsite.html bob-adams@atbi.com

Cell: J3
Comment: This cell may be left blank if appropriate data is not reported. Many companies combine Cash and Marketable Securities. If true, delete the ???.

Cell: E4
Comment: If AR is rising, investigate. Is the industry suffering them same type of increase?

Cell: C5
Comment: How quickly are customers paying for goods received. If a high number, there may be something wrong with the product.

Cell: E8
Comment: If increasing, is the increase related to a company product, or is there a slowdown in the industry?

Cell: C9
Comment: The best comparison is with other companies in the same industry. This represents the time products sit on the shelf waiting to be sold.

Cell: J9
Comment: ??? indicates data is missing and it will be necessary to get appropriate data from the Annual Report or 10K. The same is true of each cell containing 3 question marks (???).

Cell: E14
Comment: If a company invests in a new plant or equipment, sales should increase once the plant/equipment is on line. A decrease in PP&E doesn't speak well for future growth of the company.

Cell: E17
Comment: If increasing, why? Is the ROE (Sect. 2B of SSG) much higher than the intrerest rate the company has to pay on borrowed money?

Cell: E20
Comment: How many times does PreTax Profit exceed the interest paid on LT debt? If less than 3, turn the page (find another company). If less than 5 investigate -- Is the ROE (Sect. 2B of SSG) greater than the interest rate at which the company can borrow money? If the company profits only exceed the payment on interest by 2-3 times, and there is a downturn in the market, the company may collapse.

Cell: E23
Comment: If increasing, why? Small increases may represent employee options, which, if given to all employees is normally good.

Cell: E25
Comment: If the Cost of Sales is increasing, Sales should increase too.

Cell: J25
Comment: If data is taken from OPS, leave this cell blank.

Cell: J26
Comment: If data is taken from the Annual Report, leave this cell blank and delete the ???

Cell: E27
Comment: Cashflow growth shows the direction of Cashflow (increase or decrease). If it is not growing equal to or better than Sales growth, there is a problem.

Cell: E29
Comment: Free Cashflow is what's left over after all capital spending has been deducted. A margin of 10 represents a fair return on your investment.

Cell: J30
Comment: The Annual Report will show this as a negative number. Do not enter it as a negative number here.

If a "net" figure is reported, go to the 10-K or an online source where the net data is shown in detail and analyze which expenditures should increase Revenues. The attempt is to discover if capital expenditures are boosting Revenues at the same rate. Normally anything listed as "under construction" is excluded.

Cell: E31
Comment: This is a ratio between Net Income and Net Cash from Operations. How efficient is the company in producing Earnings is the question answered here. Compare to peer companies.

Cell: J31

Comment: The Annual Report will show this as a negative number. Do not enter it as a negative number here.

Cell: J33

Comment: Use MM/DD/YYYY format.

Cell: D34

Comment: Compares this year with last year.

Cell: E34

Comment: Compares this year with last year.

Cell: C36

Comment: This value represents the amount of cash purchased with each share of stock purchased, or held. There is little risk in "cash", therefore the actual risk in each share of stock is the price per share less this amount.

Cell: C39

Comment: Short-term debt is ignored. There is normally enough cash available to pay the short-term debt.

Cell: C42

Comment: A fairly severe test of the financial well being of a company. Anything better than 1 is considered acceptable.

Cell: C45

Comment: A test to determine if the company has enough Assets over Liabilities to continue their business without needing to borrow.

Cell: C48

Comment: Higher is better, but it is related to the Cost of Sales and Inventory. Too high a ratio may indicate a problem in Cost of Sales and/or Inventory.

Cell: C51

Comment: If money is spent on PP&E, Sales should increase. Plants under construction should not be included in the total as one cannot expect something under construction to increase sales.

Cell: C54

Comment: This ratio represents how much you must invest to receive one dollar worth of sales. Compare to companies in the same industry.