

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15 (d) of the
Securities Exchange Act of 1934

For the quarterly period ended June 30, 1995.

Commission File Number: 1-9249

GRACO INC.

(Exact name of Registrant as specified in its charter)

Minnesota

41-0285640

(State of incorporation)

(I.R.S. Employer Identification Number)

4050 Olson Memorial Highway
Golden Valley, Minnesota

55422

(Address of principal executive offices)

(Zip Code)

(612) 623-6000

(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, and (2) has been subject to such filing requirements for the past 90 days.

Yes X No

11,492,931 common shares were outstanding as of June 30, 1995.

GRACO INC. AND SUBSIDIARIES

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PART I

GRACO INC. AND SUBSIDIARIES

Item I. CONSOLIDATED STATEMENTS OF EARNINGS

(Unaudited)

	Thirteen Weeks Ended		Twenty-Six Weeks Ended	
	June 30, 1995	July 1, 1994	June 30, 1995	July 1, 1994
(In thousands except per share amounts)				
Net sales	\$103,402	\$94,179	\$198,929	\$175,109
Cost of products sold	51,987	49,952	100,987	92,446
Gross profit	51,415	44,227	97,942	82,663
Product development	3,941	3,566	7,862	7,122
Selling	22,068	22,789	43,758	45,088
General and administrative	10,982	10,659	22,082	20,147
Operating profit	14,424	7,213	24,240	10,306
Interest expense	745	480	1,429	848
Other expense, net	(53)	138	343	177
Earnings before income taxes	13,732	6,595	22,468	9,281
Income taxes	5,200	2,400	8,500	3,250
Net earnings	\$8,532	\$4,195	\$13,968	\$6,031
Net earnings per common and common equivalent share	\$.73	\$.36	\$1.20	\$.52
Cash dividend per common share	\$.16	\$.14	\$.32	\$.28

See notes to consolidated financial statements.

GRACO INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

	June 30, 1995	December 30, 1994
	-----	-----
ASSETS	(Unaudited)	
(In thousands)		
Current Assets:		
Cash and cash equivalents	\$1,137	\$2,444
Accounts receivable, less allowances of \$5,700 and \$4,700	82,493	75,589
Inventories	53,039	50,529
Deferred income taxes	11,890	11,755
Other current assets	2,795	3,628
	-----	-----
Total current assets	151,354	143,945
Property, plant and equipment:		
Cost	154,117	145,164
Less Accumulated Depreciation	(79,377)	(75,124)
	-----	-----
	74,740	70,040
Other assets	14,991	14,400
	-----	-----
	\$241,085	\$228,385
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Notes payable to banks	\$16,276	\$11,675
Current portion of long-term debt	5,905	5,685
Trade accounts payable	18,707	19,764
Dividends payable	1,838	1,857
Income taxes payable	2,005	5,761
Other current liabilities	42,697	44,798
	-----	-----
Total current liabilities	87,428	89,540
Long-term debt, less current portion above	26,025	26,798
Retirement benefits and deferred compensation	32,957	30,196
Shareholders' equity:		
Preferred stock	1,474	1,474
Common stock	11,486	11,377
Additional paid-in capital	20,167	18,289
Retained earnings	60,924	50,702
Other, net	624	9
	-----	-----
	94,675	81,851
	-----	-----
	\$241,085	\$228,385
	=====	=====

See notes to consolidated financial statements.

GRACO INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

Twenty-Six Weeks Ended
June 30, 1995 July 1, 1994

CASH FLOWS FROM OPERATING ACTIVITIES:

(In thousands)

Net Earnings	\$13,968	\$6,031
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	6,381	5,157
Deferred income taxes	321	(549)
Change in:		
Accounts receivable	(2,623)	(11,644)
Inventories	(1,542)	(12,868)
Trade accounts payable	(2,125)	1,895
Accrued salaries	(1,570)	(872)
Retirement benefits and deferred compensation	1,950	1,025
Other accrued liabilities	(5,438)	1,097
Other	1,449	(831)
	-----	-----
	10,771	(11,559)
	-----	-----

CASH FLOWS FROM INVESTING ACTIVITIES:

Property, plant and equipment additions	(11,189)	(7,659)
Proceeds from sale of property, plant, and equipment	260	169
Purchases of marketable securities	0	(5,464)
Proceeds from marketable securities	0	31,809
	-----	-----
	(10,929)	18,855
	-----	-----

CASH FLOWS FROM FINANCING ACTIVITIES:

Borrowing on notes payable and lines of credit	92,331	37,140
Payments on notes payable and lines of credit	(89,041)	(20,497)
Payments on long-term debt	(410)	(332)
Common stock issued	2,157	2,774
Retirement of common and preferred stock	0	(5)
Cash dividends paid	(3,765)	(34,493)
	-----	-----
	1,272	(15,413)
	-----	-----

Effect of exchange rate changes on cash	(2,421)	(401)
	-----	-----

Net decrease in cash and cash equivalents	(1,307)	8,518
---	---------	-------

Cash and cash equivalents:

Beginning of year	2,444	11,095
	-----	-----
End of period	\$1,137	\$2,577
	=====	=====

See notes to consolidated financial statements.

GRACO INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. The consolidated balance sheet of Graco Inc. and Subsidiaries (the Company) as of June 30, 1995, and the related statements of earnings and cash flows for the twenty-six weeks ended June 30, 1995, and July 1, 1994, have been prepared by the Company without being audited.

In the opinion of management, these consolidated statements reflect all adjustments necessary to present fairly the financial position of Graco Inc. and Subsidiaries as of June 30, 1995, and the results of operations and cash flows for all periods presented.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. Therefore, these statements should be read in conjunction with the financial statements and notes thereto included in the Company's 1994 Form 10-K.

The results of operations for interim periods are not necessarily indicative of results which will be realized for the full fiscal year.

2. Major components of inventories were as follows:

(In thousands)	June 30, 1995	Dec. 30, 1994
	-----	-----
Finished products and components	\$48,013	\$46,694
Products and components in various stages of completion	28,024	24,826
Raw materials	12,237	13,918
Reduction to LIFO cost	(35,235)	(34,909)
	-----	-----
	\$53,039	\$50,529
	=====	=====

Item 2. GRACO INC. AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Results of Operations

Net earnings in the second quarter of \$8,532,000 increased \$4,337,000 from the same period a year ago as the Company's sales continue to improve in Europe and the Pacific offset by the recent softening of sales in the North American markets. In addition to increased sales, gross margin levels have improved from 1994 and operating expenses as a percent of sales have declined due primarily to cost reduction efforts initiated in 1994.

Sales in the second quarter of \$103,402,000 increased \$9,223,000, or 10 percent, from the same period in 1994. Second quarter sales in the Americas decreased 4 percent to \$63,847,000, and European sales were up 40 percent to \$21,085,000 (a 23 percent volume increase, and a 17 percent gain due to exchange rates). In the Pacific (excluding Japan), sales increased 43 percent to \$8,619,000 (a 41 percent volume increase, and a gain of 2 percent on exchange rates). In Japan, sales increased 48 percent to \$9,851,000 (a 21 percent volume increase and a gain of 27 percent on exchange rates).

Sales for the six months were \$198,929,000, a 14 percent increase over the same period last year. In the Americas, sales increased 3 percent to \$128,962,000. European sales were up 38 percent to \$37,327,000 (a volume increase of 23 percent and a 15 percent gain due to exchange rates). Sales in the Pacific (excluding Japan) increased 59 percent to \$17,161,000 (a 57 percent volume increase and a 2 percent gain due to exchange rates). In Japan sales increased 28 percent to \$15,479,000 (a 9 percent volume increase and a 19 percent gain on exchange rates).

Operating expenses in the second quarter of \$36,991,000 are at approximately the same level as the second quarter of 1994. Product development expense increased 11 percent over 1994, as previously announced new product initiatives continue. Selling expenses were 3 percent lower than the same period last year, largely due to lower headcount levels. General and administrative costs were up by 3 percent, due primarily to expense items related to increased profitability.

The effective income tax rate for the quarter was 38 percent compared to 36 percent for the same period in 1994. The increase was due primarily to foreign results effectively taxed at higher rates.

For the second quarter, consolidated bookings were up 2 percent. Bookings declined in the Americas, but were up sharply in Europe, the Pacific and Japan. Backlog at June 30, 1995 was \$27,000,000, approximately 3 percent lower than it was in the previous quarter and 9 percent lower than the second quarter of 1994.

The Company expects favorable sales and order trends in Europe and the Pacific region as these economies strengthen. The slowing of the U.S. economy will continue to impact domestic bookings and backlog during the second half of 1995. The Company will make further investments in improvements to manufacturing efficiency and new product development, while closely controlling expenses throughout the organization.

Financial Condition

Cash was used for operating activities and fixed asset additions. Accounts receivable increased \$6,904,000 from the prior year-end due to the increased sales volume, and inventories increased \$2,510,000 primarily in production. Property, plant and equipment was purchased year-to-date totaling \$11,189,000.

The Company has unused lines of credit available at June 30, 1995, totaling \$47 million.

PART II

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

At the Annual Meeting of Shareholders held on May 2, 1995, Dale R. Olseth, Charles M. Osborne, and William G. Van Dyke were elected to the Office of Director with the following votes:

	For -----	Withheld -----
Dale R. Olseth	10,471,622	23,846
Charles M. Osborne	10,483,868	11,600
William G. Van Dyke	10,484,964	10,504

At the same meeting, the selection of Deloitte & Touche as independent auditors for the current year was approved and ratified, with the following votes:

For -----	Against -----	Abstentions -----	Broker Non-Vote -----
10,398,535	86,574	10,358	0

No other matters were voted on at the meeting.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

1995 Corporate and Business Unit Annual Bonus Plan	Exhibit 10
Statement on Computation of Per Share Earnings	Exhibit 11
Financial Data Schedule	Exhibit 27

(b) No reports on Form 8-K have been filed during the quarter for which this report is filed.

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.

GRACO INC.

Date: August 7, 1995

By: /S/David A. Koch
David A. Koch
Chairman and Chief Executive Officer

Date: August 8, 1995

By: /S/David M. Lowe
David M. Lowe
Treasurer
(Principal Financial Officer)

GRACO INC.
1995 CORPORATE
&
BUSINESS UNIT
ANNUAL BONUS PLAN

Effective January 1, 1995
Human Resources

GRACO INC.
CORPORATE & BUSINESS UNIT
ANNUAL BONUS PLAN

Objectives

- - To create shareholder value through achievement of annual financial objectives.
- - To motivate and retain those key executives and managers who work in positions where they can impact the Company's annual financial objectives.

Plan Design

The Plan links the size of each individual's award to specific financial objectives. These objectives are tailored for the Corporation and for each Business Unit. These objectives are:

- - Corporation
 - Corporate earnings
- - Business Units
 - Profitability objective

Eligibility Requirements

Only those positions which carry clear managerial responsibility for directly contributing to Graco's Corporate earnings objective and Business Unit profitability and sales objectives are eligible to be included in this Plan.

Only those individuals in eligible positions who have demonstrated and are maintaining a performance level that meets the supervisor's normal expectations for that position are eligible for annual participation in this Plan as well as the receipt of any annual Bonus Payments.

Participation

The top executive in each organizational unit may nominate managers for participation in this Plan when the established position and individual eligibility requirements have been met.

The Management Organization and Compensation Committee of the Graco Inc. Board of Directors has sole authority to approve the participation of the Chief Executive Officer in the Plan.

The Chief Executive Officer of Graco Inc. has sole authority to select and approve all other Plan participants.

Bonus Maximum

Taken in conjunction with base salary market comparisons, bonus maximum for all positions will be:

- Commensurate with the position's ability to impact the annual Corporate earnings objective and Business Unit profitability and sales objectives.
- Consistent with total compensation levels prevalent for similar positions in the market place.

Based on these criteria, bonus maximums ranging from 10% to 80% have been established for each individual.

Bonus Payment

The determination of a participant's annual Bonus Payment will be calculated by adding the bonus results attained for Corporate earnings performance (expressed in percent) to the bonus results attained for any applicable Business Unit's contribution or margin growth performance (expressed in percent). These bonus results are then multiplied by the participant's Maximum Bonus Percentage and then multiplied by the participant's Base Salary for the Plan Year, to determine the total Bonus Payment.

Example:

Annual Corporate Performance Results	+	Annual Business Unit Performance Results (if applicable)	X	Participant's Maximum Bonus Salary	X	Participant's Annual Base Salary	=	Bonus
%		%		\$		\$		\$

Administration

The following rules have been established to insure equitable administration of Graco's Annual Bonus Plan (the Plan):

1. The Plan will be administered by the Management Organization and Compensation Committee of the Board of Directors. The Committee may cancel the Plan and interpret the Plan.
2. The Management Organization and Compensation Committee shall establish the annual corporate bonus plan financial objectives. Within the basic framework of the Plan, the Chief Executive Officer may establish the annual bonus plan financial objectives for individual Business Units. The CEO may also establish deadlines for filing administrative forms and adopt other administrative rules.

The CEO has established the Bonus Administrative Committee consisting of the President, the Vice President, Human Resources, and the Compensation Manager. This Committee is responsible for making approval recommendations on all Annual Bonus Program administrative matters, such as participation award payments, performance measures, and performance results. All requests for adjustments or exceptions are to be formally submitted to this Committee for review through the Compensation Manager.

3. Key executives and managers selected to participate in the Plan after its annual effective date (January 1st) may be included on a pro-rata basis.
4. Participation in the Plan one year does not necessarily assure participation in subsequent years. Eligibility requirements for both the position and individual performance must be met continually.
5. Participation continues during any paid time off such as short term disability (up to six months). Participation ceases with retirement, death, or long term disability (over six months). In the event participation ceases due to retirement, death, or long term disability, the Participant will be eligible for a Bonus Payment, calculated using the Maximum Bonus Percent and Base Salary up to the time of retirement, death, or long term disability and the annual performance results for the year in which retirement, death, or long term disability occurs.
6. A participant who transfers to a position not eligible for inclusion in the Plan will be eligible for a pro-rata award based on the actual time employed in the eligible position during the year. The pro-rated award will be paid as described in Administrative Rule #11.

7. A participant who resigns or is terminated effective during the Plan Year is ineligible for a bonus.

Participants must maintain satisfactory performance throughout the Plan year in order to be eligible to receive a bonus award payment.

In addition, a participant whose employment termination has been requested due to performance or otherwise for cause will be ineligible for a bonus payment even though the participant is still employed at year-end.

8. Corporate earnings calculations will include such effects as those created by foreign exchange gain/loss translation and income tax rate changes.
9. Corporate earnings calculations will be based on actual exchange rates, not plan rates.
10. Acquisitions and divestitures not included in the annual business plan for the Plan Year will be excluded from the corporate earnings calculations.
11. Significant changes in historical FASB accounting practices or income tax rates will be included in corporate earnings calculations at the discretion of the Management Organization and Compensation Committee of the Board of Directors.
12. Payments will be made by March 15th of the year following each successive Corporate and Business Unit performance year.

GRACO INC. AND SUBSIDIARIES

COMPUTATION OF NET EARNINGS PER COMMON SHARE

(Unaudited)

	Thirteen Weeks Ended		Twenty-Six Weeks Ended	
	June 30, 1995	July 1, 1994	June 30, 1995	July 1, 1995
	(In thousands except per share amounts)			
Net earnings applicable to common stock:				
Net earnings	\$8,532	\$4,195	\$13,968	\$6,031
Less dividends on preferred stock	19	19	37	37
	<u>\$8,513</u>	<u>\$4,176</u>	<u>\$13,931</u>	<u>\$5,994</u>
	=====	=====	=====	=====
Average number of common and common equivalent shares outstanding:				
Average number of common shares outstanding	11,489	11,514	11,453	11,514
Dilutive effect of stock options computed on the treasury stock method	147	49	115	57
	<u>11,636</u>	<u>11,563</u>	<u>11,568</u>	<u>11,571</u>
	=====	=====	=====	=====
Net earnings per common share and common equivalent share	<u>\$0.73</u>	<u>\$0.36</u>	<u>\$1.20</u>	<u>\$0.52</u>
	=====	=====	=====	=====

Primary and fully diluted earnings per share are substantially the same.

THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM GRACO INC. AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF EARNINGS AND CONSOLIDATED BALANCE SHEETS FOR THE QUARTERLY PERIOD ENDING JUNE 30, 1995 AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.

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GRACO INC.
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6-MOS		
	DEC-29-1995	
	JUN-30-1995	
		1,137
		0
		88,188
		5,695
		53,039
	151,354	
		154,117
	79,377	
	241,085	
	87,428	
		31,930
		11,486
	1,474	
		0
		81,715
241,085		
		198,929
	198,929	
		100,987
		100,987
	75,474	
	1,132	
	1,429	
	22,468	
		8,500
	13,968	
		0
		0
		0
		13,968
		1.20
		1.20