Hesston Corporation stockholder report

This report represents the financial and directors of the Hesston Corporation for the stub period ending on December 31, 1978. This publication funded by the National Historical Publications and Records Commission through the Kansas State Historical Records Advisory Board.

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HESSTON CORPORATION

Stub Period Report To Stockholders

For the Three Months Ended
December 31, 1978

Financial Highlights

	Three months ended December 31, 1978	Years ended September 30, 1978	1977
	(000's Omitted)		
Net sales	**$ 39,392**	$165,996	$142,245
Loss before income taxes and extraordinary item	**$ (2,901)**	$ (7,255)	$ (17,272)
Provision for income tax benefit	—	2,633	7,956
Loss before extraordinary item	**(2,901)**	(4,622)	(9,316)
Extraordinary item	—	878	—
Net loss	**$ (2,901)**	$ (3,744)	$ (9,316)
Net loss per share	**$ (.94)**	$ (1.40)	$ (4.93)
Common shares outstanding	**3,387,952**	3,387,952	3,387,952

The fiscal year-end of Hesston Corporation has been changed to December 31. This report covers the three month period ended December 31, 1978.

The next Annual Meeting of Stockholders of Hesston Corporation will be held in April of 1980.

A copy of Hesston Corporation's annual report to the Securities and Exchange Commission (Form 10-K) may be obtained by writing to Hesston Corporation, Attention: Mr. Richard F. Hrdlicka, Secretary, Hesston, Kansas 67062.

New York Stock Exchange - HES, HES Pr

HESSTON CORPORATION
HESSTON, KANSAS 67062, Phone: (316) 327-4000

To Our Shareholders:

As reported previously, the Company's year-end was changed from September 30 to December 31. This report covers the "stub period" from October 1, 1978 to December 31, 1978, as well as financial information for years ended September 30, 1978 and 1977. Results of operations for a period of less than a year are not necessarily indicative of the results for a full year. This change was made so that financial reporting will more nearly fit the natural business year and to facilitate other statistical reporting.

Management's Discussion and Analysis of the Summary of Operations

To assist in reviewing Management's discussion and analysis of the summary of operations, certain financial information is summarized below (000's omitted):

	Three months ended December 31,		Years ended September 30,		
	1978	1977 (Unaudited)	**1978**	**1977**	**1976**
Net sales	**$ 39,392**	$25,276	$165,996	$142,245	$187,194
Cost of sales	**27,853**	18,659	113,473	101,419	125,560
Operating expenses	**11,543**	10,417	43,740	40,369	47,547
Interest & finance charges	**3,319**	2,603	13,752	17,527	19,388
Income tax expense (benefit)		(2,455)	(2,633)	(7,956)	121
Net (loss)	**(2,901)**	(4,156)	(3,744)	(9,316)	(6,152)

Three month period ended December 31, 1978 vs. December 31, 1977

Sales and results of operations

The increase in sales was due to increased shipments to dealers in North America. This increase occurred because dealer inventories at the beginning of the quarter were significantly lower in 1978 than 1977. The higher gross profit accompanying the increased sales was the primary reason for the reduced loss in 1978.

Cost of sales

The cost of sales percentage was 70.7% in 1978 compared to 73.8% in 1977. The reduced cost of sales was due to increased production efficiencies associated with the higher volume of sales and production and to a more favorable product and customer mix of sales.

Operating expenses

The Company held operating expenses to a 10.8% increase over 1977 levels, despite the sales increase and inflationary pressures. These expenses were 29.3% of sales in 1978 compared to 41.2% in 1977.

Interest and finance charges

The 27.5% increase in interest and finance charges was due to an increase in wholesale shipments to dealers in North America. As is typical in the farm equipment industry, Hesston Corporation provides the floorplan and pays most of the financing costs for inventories at dealers. The finance expense is recognized at the time of sale. In addition, short-term interest rates in the United States were higher in 1978 than 1977. These increases were partially offset by a reduction in interest paid on long-term debt.

Income taxes

In 1978, the Company received no income tax benefit because available loss carrybacks have been fully utilized in the United States.

Year-ended September 30, 1978 vs. September 30, 1977

Sales and results of operations

The increase in sales was due to an upturn in the farm economy in the major markets of North America and Europe. Increased retail sales of farm equipment by dealers in the U.S. and Canada resulted in a reduction of dealer inventories of approximately $26,000,000 as well as higher wholesale shipments. These increased sales and reduced interest and finance charges were the primary reasons for the reduced loss in 1978.

Cost of sales

The cost of sales percentage declined to 68.4% in 1978 compared to 71.3% in 1977. This improvement was the result of better plant utilization in the current year and a reduced level of sales discounts.

Operating expenses

The Company made progress during 1978 in the management of operating expenses. In fact, the level of operating expenses in real terms remained constant despite the sales increase. However, the upward inflationary pressure caused the operating expenses to increase 8.4%. These expenses were 26.3% of sales in 1978 compared to 28.4% in 1977.

Interest and finance charges

The lower interest was due to reduced levels of long-term and short-term borrowing as well as lower finance charges to carry inventory at dealers.

Income taxes

The effective tax benefit rate in 1978 was 36.3%, excluding the tax benefit reported as an extraordinary item, compared to 46.1% in 1977. The reduction occurred because a greater portion of the current losses were in countries for which no tax loss carryback was available. In 1978, an additional tax benefit of $878,000, or 12.1%, resulted from offsetting prior years' losses against the current year's taxable income. This tax benefit was reported as an extraordinary item in 1978.

Year-ended September 30, 1977 vs. September 30, 1976

Sales and results of operations

The decline in sales reflected lower shipments to dealers in North America. This decline was caused by a planned reduction in Hesston dealer inventory, as well as lower retail sales by dealers to farmers and ranchers, as was generally true throughout the farm equipment industry. The downturn in industry sales was related to the low prices for beef and grains and unfavorable weather conditions in several parts of North America. The amount of Hesston equipment at dealers declined by approximately $15,000,000. Sales outside North America increased to $32,579,000 in 1977 compared to $25,064,000 in 1976.

Cost of sales

Cost of sales increased to 71.3% in 1977 compared to 67.1% in 1976. This increase was a result of giving larger sales discounts in 1977 and a decrease in production at two of our plants which caused fixed production costs to increase as a percentage of sales.

Operating expenses

This decrease included the reductions associated with the closing of two plants in 1977. In addition, the Company reduced operating expenses. However, operating expenses were 28.4% of sales in 1977 compared to 25.4% in 1976. This increase as a percentage of sales was due to the inability to cut operating expenses in the same percentage as the sales decrease.

Interest and finance charges

In 1977, interest and finance charges were 12.3% of sales compared to 10.4% in 1976.

Hesston Corporation stockholder report

Income taxes

The effective tax benefit rate was 46.1% in 1977 compared to 23.3% in 1976. Most of the 1977 tax loss occurred in countries where current year taxable loss could be carried back against prior years' taxable income. In 1976, a significant portion of the taxable loss could not be offset against prior years' income.

Other Information

PERCENTAGE OF NET SALES BY PRODUCT LINE

(Each class of similar products which individually accounted for 10% or more of sales)	Three months ended December 31, 1978	Years ended September 30, 1978	1977	1976	1975	1974
Hay handling equipment	22%	17%	12%	28%	38%	36%
Windrowers	27%	27%	37%	33%	25%	24%
Forage harvesters	19%	20%	23%	16%	15%	15%
Rotary mowers	12%	16%	16%	12%	10%	11%
Other	20%	20%	12%	11%	12%	14%

The Company is principally engaged in the farm equipment business (see Note 14 of Notes to Consolidated Financial Statements for 1978 industry segment information). The percentage of net sales applicable to farm equipment products for the period 1977 - 1974 was as follows: 1977 - 96%, 1976 - 99%, 1975 - 96%, 1974 - 96%. 100% of the loss in 1977 and 86% of the loss from continuing operations in 1976 and all of the income before income taxes for the two previous years was from farm equipment sales.

PRICE RANGE OF COMMON AND $1.60 PREFERRED STOCK

	Common Stock High	Common Stock Low	$1.60 Preferred Stock High	$1.60 Preferred Stock Low
Fiscal year-ended September 30, 1977				
First Quarter	10	7-3/4	17-3/4	15-1/2
Second Quarter	12	8-1/4	19-1/4	16-1/4
Third Quarter	10-1/2	8	18	16
Fourth Quarter	9	6-7/8	17	14
Fiscal year-ended September 30, 1978				
First Quarter	7-3/8	5-7/8	16-1/4	14-1/4
Second Quarter	6-1/4	5-1/2	15-1/8	14-1/8
Third Quarter	8-7/8	5-7/8	17	14-3/4
Fourth Quarter	13-1/4	7-1/8	18-3/8	15-1/4
Three months ended December 31, 1978	11	7	18	14-1/2

Ten Year Summary of Operations

(Dollars in thousands except per share amounts)

	Three months ended December 31, 1978	1978	1977
Statement of Operations			
*Net sales	$ 39,392	$165,996	$142,245
*Cost of sales	27,853	113,473	101,419
*Operating expenses	11,543	43,740	40,369
*Interest & finance charges	3,319	13,752	17,527
*Provision (credit) for income taxes	—	(2,633)	(7,956)
Income (loss) before other credits (charges)	(2,901)	(4,622)	(9,316)
Other credits (charges) to income (see note)		878	—
Net income (loss)	(2,901)	(3,744)	(9,316)
Primary earnings (loss) per common share	(.94)	(1.40)	(4.93)
Fully diluted earnings (loss) per common share		—	—
Depreciation	1,280	4,725	4,979
*Earnings (loss) as a % of net sales	(7.4%)	(2.8%)	(6.5%)
Dividends, Equity, Net Book Value			
Dividends:			
Common Stock		—	—
Per share of Common Stock		—	—
$1.60 Preferred Stock	200	800	800
Per share of $1.60 Preferred Stock	.40	1.60	1.60
$.60 Preferred Stock	90	169	—
Per share of $.60 Preferred Stock	.15	.2815	—
Total equity	49,656	52,847	57,560
Book value per common share	8.98	9.92	11.30
Average common shares outstanding	3,387,952	3,387,952	2,053,157
*Return on average equity	(5.7%)	(8.4%)	(17.7%)
Other Data			
Year-end assets	143,586	140,859	150,035
Net property, plant and equipment	33,774	33,866	36,949
Working capital	50,739	53,479	56,470
Long-term debt (excluding current maturities)	34,467	35,157	37,978
Current ratio	1.9/1	2.1/1	2.1/1
Average asset turn	1.11	1.14	.93
Year-end long-term debt/equity	.69	.67	.64
Stock price range - Common	11-7	13¼-5½	12-6⅞
Stock price range-$1.60 Preferred	18-14½	18⅜-14⅛	19¼-14
Average employment	3,128	3,084	3,149

*Amounts are from continuing operations before other credits (charges).

NOTE: Other credits (charges) to income include a credit in 1978 for a reduction of income taxes arising from utilization of prior years' losses. Charges are included in 1976 - 1972 for discontinued operations. The prior period effect of a change in costing inventory in the amount of $1,297,000 is included in 1975. If the new inventory costing method had been applied retroactively in 1975, the net income would have been $8,275,000 and primary earnings per common share would have been $3.95. The effect of this change for the other periods shown would not be significant.

Hesston Corporation stockholder report

Years ended September 30,

1976	1975	1974	1973	1972	1971	1970	1969
$187,194	$205,922	$151,337	$ 96,431	$ 60,882	$ 44,955	$ 41,245	$ 38,490
125,560	130,434	96,534	60,050	38,213	27,970	27,439	25,247
47,547	43,360	31,619	20,840	14,012	10,843	9,829	8,701
19,388	16,840	7,159	3,355	2,778	2,717	1,953	1,358
121	7,266	7,564	5,871	2,905	1,749	1,130	1,695
(4,128)	8,907	8,659	6,466	3,050	—	—	—
(2,024)	665	(409)	(289)	(24)	—	—	—
(6,152)	9,572	8,250	6,177	3,026	1,762	994	1,521
(3.50)	4.60	4.15	3.48	1.85	1.08	.61	.93
—	4.23	—	—	—	—	—	—
5,461	4,263	2,244	1,607	1,046	1,063	1,010	908
(2.2%)	4.3%	5.7%	6.7%	5.0%	3.9%	2.4%	4.0%
1,192	994	636	479	402	402	402	362
.60	.50	.32	.28	.27	.27	.27	.27
800	360	—	—	—	—	—	—
1.60	.72	—	—	—	—	—	—
—	—	—	—	—	—	—	—
—	—	—	—	—	—	—	—
47,998	56,142	36,243	28,629	16,019	13,301	11,914	11,316
17.86	21.96	18.23	14.40	9.78	8.12	7.27	6.91
1,987,839	1,987,747	1,987,747	1,775,829	1,637,747	1,637,747	1,637,747	1,637,747
(7.9%)	19.3%	26.7%	29.0%	20.8%	13.9%	8.5%	14.0%
157,470	161,641	115,201	57,379	35,753	27,166	27,748	21,770
40,364	44,193	30,870	17,049	9,150	6,686	6,950	6,142
47,223	60,758	41,867	18,789	14,191	13,351	10,765	9,860
43,095	47,524	37,060	7,781	8,069	7,094	6,084	4,941
1.7/1	2.1/1	2.0/1	1.9/1	2.2/1	3.0/1	2.1/1	2.8/1
1.17	1.50	1.79	2.11	1.95	1.64	1.67	1.90
.90	.85	1.02	.27	.50	.53	.51	.44
23⅝-9½	27⅞-14¼	36⅛-14¼	46¾-15½	26-11⅝	11¾-6⅛	10-4⅞	13½-7⅝
25½-16	30⅜-24⅛						
3,850	4,581	3,397	2,490	1,634	1,371	1,478	1,378

Consolidated Balance Sheet

Assets

	December 31, 1978	September 30, 1978	September 30, 1977
	(000's Omitted)		
Current assets:			
Cash	$ 1,414	$ 4,860	$ 4,297
Accounts receivable	22,092	26,431	23,469
Advance to unconsolidated credit subsidiary (Note 3)			8,264
Refundable income taxes (Note 7)	4,649	4,599	7,200
Inventories:			
Finished goods	31,357	26,793	27,779
Parts	13,143	11,867	9,482
Work in process	15,789	12,667	9,845
Raw materials	12,957	11,727	12,424
	73,246	63,054	59,530
Other current assets (Notes 4 and 7)	5,092	3,871	4,826
Total current assets	106,493	102,815	107,586
Investment in unconsolidated credit subsidiary (Note 3)	465	462	581
Other assets (Note 4)	2,854	3,716	4,919
Property, plant and equipment:			
Land	1,002	968	982
Buildings	27,472	26,939	26,833
Machinery and equipment	26,641	26,101	24,979
Office furniture and fixtures	3,329	3,292	3,309
Transportation equipment	2,054	2,118	3,249
	60,498	59,418	59,352
Less accumulated depreciation	26,724	25,552	22,403
Net property, plant and equipment	33,774	33,866	36,949
	$143,586	$140,859	$150,035

Hesston Corporation stockholder report

Liabilities and Stockholders' Equity

(000's Omitted)	December 31, 1978	September 30, 1978	September 30, 1977
Current liabilities:			
Notes payable to banks (Note 5)	$ 19,006	$ 13,131	$ 14,613
Accounts payable	13,671	12,445	10,643
Accrued sales finance costs and discounts	11,270	11,336	12,523
Accrued payroll, profit-sharing and retirement contributions (Note 10)	3,046	3,509	3,427
Other accrued liabilities	5,418	5,692	5,277
Long-term debt payable within one year	3,343	3,223	4,633
Total current liabilities	55,754	49,336	51,116
Long-term debt payable after one year (Note 6)	34,467	35,157	37,978
Deferred income taxes and other (Note 7)	3,709	3,519	3,381
Contingencies (Note 11)			
Stockholders' equity (Notes 2, 6, 8 and 9):			
Preferred stock, $2 par value, 2,000,000 shares authorized:			
$1.60 cumulative convertible preferred stock, 499,800 shares outstanding, aggregate liquidation value $12,495,000	1,000	1,000	1,000
$.60 cumulative convertible preferred stock, 600,000 shares outstanding, aggregate liquidation value $6,000,000	1,200	1,200	1,200
Common stock, $2 par value, 8,000,000 shares authorized, 3,387,952 shares outstanding	6,775	6,775	6,775
Capital in excess of par value	33,996	33,996	33,996
Retained earnings	6,685	9,876	14,589
Total stockholders' equity	49,656	52,847	57,560
	$143,586	$140,859	$150,035

See summary of accounting policies and notes.

Consolidated Statement of Operations

	Three months ended December 31, 1978	Years ended September 30, 1978	Years ended September 30, 1977
	(000's Omitted)		
Net sales	$ 39,392	$165,996	$142,245
Cost of sales	27,853	113,473	101,419
Gross profit	11,539	52,523	40,826
Operating expenses:			
Marketing and selling	5,730	20,870	18,966
General and administrative	4,628	18,283	16,776
Engineering	1,185	4,587	4,627
	11,543	43,740	40,369
Operating profit (loss)	(4)	8,783	457
Other (income) deductions:			
Interest and finance charges	3,319	13,752	17,527
Net (income) loss of credit subsidiaries (Note 3)	(3)	119	(126)
Other - net (Note 14)	(419)	2,167	328
	2,897	16,038	17,729
Loss before income taxes and extraordinary item	(2,901)	(7,255)	(17,272)
Provision (benefit) for income taxes (Note 7):			
Current		(4,599)	(7,343)
Deferred		1,088	(613)
Charge equivalent to tax benefit of loss carryforward		878	
		(2,633)	(7,956)
Loss before extraordinary item	(2,901)	(4,622)	(9,316)
Extraordinary item - reduction of income taxes arising from utilization of prior years' losses (Note 7)		878	
Net loss	$ (2,901)	$ (3,744)	$ (9,316)
Loss per common share:			
Loss before extraordinary item	$ (.94)	$ (1.66)	$ (4.93)
Extraordinary item		.26	
Net loss	$ (.94)	$ (1.40)	$ (4.93)

See summary of accounting policies and notes.

Consolidated Statement of Stockholders' Equity

(000's Omitted)

	$1.60 Preferred stock, $2 par value	$.60 Preferred stock, $2 par value	Common stock, $2 par value	Capital in excess of par value	Retained earnings	Total
Balance, September 30, 1976	$ 1,000		$ 3,975	$18,318	$24,705	$47,998
Net loss					(9,316)	(9,316)
$.60 Preferred stock issued for cash - 600,000 shares (Note 2)		$ 1,200		4,703		5,903
Common stock issued for cash - 1,400,000 shares (Note 2)			2,800	10,975		13,775
Less cash dividends:						
$1.60 Preferred stock - $1.60 per share					(800)	(800)
Balance, September 30, 1977	$ 1,000	$ 1,200	$ 6,775	$33,996	$14,589	$57,560
Net loss					(3,744)	(3,744)
Less cash dividends:						
$1.60 Preferred stock - $1.60 per share					(800)	(800)
$.60 Preferred stock - $.2815 per share (Note 8)					(169)	(169)
Balance, September 30, 1978	$ 1,000	$ 1,200	$ 6,775	$33,996	$ 9,876	$52,847
Net loss					(2,901)	(2,901)
Less cash dividends:						
$1.60 Preferred stock - $.40 per share					(200)	(200)
$.60 Preferred stock - $.15 per share					(90)	(90)
Balance, December 31, 1978	$ 1,000	$ 1,200	$ 6,775	$33,996	$ 6,685	$49,656

See summary of accounting policies and notes.

Consolidated Statement of Changes in Financial Position

(000's Omitted)

	Three months ended December 31, 1978	Years ended September 30, 1978	Years ended September 30, 1977
Source of funds:			
Decrease in purchase commitment cash deposit (Note 4)	$ 581	$1,106	
Proceeds from long-term debt (Note 6)		3,000	
Issuance of common and preferred stock, net of issuance expenses of $322,000 (Note 2)			$19,678
Liquidation of Hesston Credit Corporation (Note 3)			2,646
Sale of assets not used in operations	272		2,335
Other	9	97	
Total funds provided	862	4,203	24,659
Application of funds:			
Operations:			
Loss before extraordinary item	2,901	4,622	9,316
Nonfund transactions:			
Depreciation	(1,280)	(4,725)	(4,979)
Noncurrent deferred income taxes and other	(190)	(138)	(456)
Undistributed income (loss) of credit subsidiaries	3	(119)	(19)
	1,434	(360)	3,862
Extraordinary item - reduction of income taxes		(878)	
Funds consumed (provided) by operations	1,434	(1,238)	3,862
Net additions to property, plant and equipment	1,188	1,642	2,665
Investment in Hesston Credit, Ltd.			600
Decrease in long-term debt	690	5,821	5,117
Dividends paid	290	969	800
Purchase commitment cash deposit (Note 4)			1,687
Other			681
Total funds consumed	3,602	7,194	15,412
Increase (decrease) in working capital	$ (2,740)	$(2,991)	$ 9,247
Increase (decrease) in components of working capital:			
Current assets:			
Cash	$ (3,446)	$ 563	$ 1,589
Receivables and advances	(4,339)	(7,903)	6,947
Inventories	10,192	3,524	(10,129)
Other	1,271	(955)	(1,496)
	3,678	(4,771)	(3,089)
Current liabilities:			
Notes payable to banks	5,875	(1,482)	(14,810)
Accounts payable	1,226	1,802	764
Accrued liabilities	(803)	(690)	1,259
Long-term debt payable within one year	120	(1,410)	451
	6,418	(1,780)	(12,336)
Increase (decrease) in working capital	$ (2,740)	$(2,991)	$ 9,247

See summary of accounting policies and notes.

Summary of Accounting Policies

Principles of consolidation - The consolidated financial statements include the accounts of the Company and its subsidiaries, except for its credit subsidiaries (Note 3), Hesston Credit Corporation and Hesston Credit, Ltd., which are reported on the equity method. All material intercompany accounts and transactions have been eliminated.

Inventories - Inventories are stated at the lower of cost (first-in, first-out basis) or market. Market represents replacement cost in the case of raw materials and net realizable value in the case of other inventories.

Property, plant and equipment - Property, plant and equipment are recorded at cost. For financial reporting purposes substantially all plant and equipment are depreciated on a straight-line basis. For income tax purposes all plant and equipment are depreciated on an accelerated method. Estimated useful lives for purposes of depreciation are as follows:

Buildings	15-40 years
Machinery and equipment	3-15 years
Office furniture and fixtures	3-10 years
Transportation equipment	3- 8 years

Expenditures for property and equipment which substantially increase the useful life of the asset are capitalized. Maintenance, repairs and minor improvements are expended as incurred. Upon sale or retirement of fixed assets, the asset cost and related accumulated depreciation are eliminated from the accounts and the gain or loss is recognized.

Income taxes - Income taxes have not been provided on a portion of the income of the Company's Domestic International Sales Corporation because the Company intends to defer the distribution of such income (approximately $2,429,000 at December 31, 1978) indefinitely.

Investment tax credits are applied as a reduction of income taxes on the flow-through method.

Sales and financing costs - Sales are recognized at the time of shipment to dealers. Under the Company's sales terms, certain financing costs are incurred beyond the date of sale. Estimated financing costs and sales discounts are accrued at the time of sale. Such estimates involve certain assumptions regarding carrying periods, future interest rates and sales programs. These are reviewed and adjusted quarterly.

Loss per common share - Loss per share is based on the weighted average number of common shares outstanding during the period (3,387,952 for the three months ended December 31, 1978 and the year ended September 30,1978, and 2,053,157 for the year-ended September 30, 1977) after giving effect to the dividend requirements of the $1.60 and $.60 Cumulative Convertible Preferred Stock (Note 8). Fully diluted per share amounts are not presented since conversion of the preferred stock or the exercise of the common stock options (Note 9) would have an antidilutive effect for the periods presented.

Notes to Consolidated Financial Statements

1. Fiscal Year Change

Effective January 1,1979, the Company changed its fiscal year from one ending September 30 to a calendar year ending December 31. These financial statements include the three month period ended December 31, 1978.

2. Sale of Company stock

In September 1977, the Company sold 2,000,000 shares of voting securities to Internazionale Holding Fiat S.A. (IHF), a wholly owned Swiss subsidiary of Fiat S.p.A. This sale was comprised of 1,400,000 shares of previously unissued Common Stock and 600,000 shares of previously unissued voting $.60 Cumulative Convertible Preferred Stock and resulted in IHF owning a controlling interest (50.2%) of the voting securities of the Company. The stock was sold for $10 per share and the excess over par value of $15,678,000 (net of $322,000 issue expenses) was credited to capital in excess of par value. IHF also has an option to purchase an additional 615,000 shares of common stock at the current market price at the date of exercise.

3. Credit subsidiaries

Hesston Credit, Ltd. (HCL), a wholly owned subsidiary, was formed in February 1977 to provide floorplan financing for Hesston farm equipment dealers in Canada. Condensed financial information for HCL is as follows:

	(000's Omitted)		
	December 31,	September 30,	
FINANCIAL POSITION	1978	1978	1977
Assets			
Cash	$ 65	$ 110	$ 12
Finance receivables	4,700	4,164	8,908
Other assets	65	66	176
	$ 4,830	$4,340	$9,096
Liabilities and equity			
Notes payable to banks	$ 4,318	$3,768	$ 233
Advances from affiliates			8,264
Other liabilities	47	110	18
Capital stock	600	600	600
Deficit	(135)	(138)	(19)
	$ 4,830	$4,340	$9,096

	Three months ended	Years ended September 30,	
OPERATIONS	December 31, 1978	1978	1977
Interest and other income	$ 154	$ 772	$ 747
Costs and expenses			
Interest	127	627	561
General and administrative	15	109	133
Other, including translation loss	5	65	47
Income taxes	4	90	25
	151	891	766
Net income (loss)	$ 3	$ (119)	$ (19)

3. Credit Subsidiaries (continued)

Hesston Corporation guarantees all borrowings of HCL and makes loans and advances to HCL.

In June 1977, the floorplan accounts receivable of Hesston Credit Corporation (HCC) were sold to an independent finance company and HCC's operations were terminated. HCC had net income of $145,000 prior to its liquidation.

4. Other assets

The Company had $955,000, $880,000 and $1,900,000 at December 31, 1978 and September 30, 1978 and 1977 respectively on deposit for a bank guarantee on a purchase commitment made to a foreign trading company in Hungary. Specific portions of the restricted cash deposit are released as performance conditions of the contract are met. Of this amount $581,000 and $1,687,000 have been classified as a non-current asset at September 30, 1978 and 1977.

At December 31, 1978, September 30, 1978 and 1977 respectively, the Company had $272,000, $544,000 and $466,000 of assets being held for resale. These assets are not presently being used in the Company's operations.

A substantial portion of the remaining balance consists of property and equipment, of a previously discontinued division, having a net book value of $1,540,000. These assets have been leased to an independent party who has assumed the Company's obligation under the terms of the original lease agreement until May 1984.

5. Short-term bank borrowings

The Company and Hesston Credit, Ltd., separately, have loan agreements with several banks (the Revolving Credit Agreement - Note 6) providing a fixed maximum commitment for short-term borrowings. Short-term borrowings under these agreements, which expire March 31, 1979, bear interest at the rate of 110% of prime for Hesston Corporation and 115% of prime for Hesston Credit, Ltd. Subsequent to December 31,1978, the Company and HCL amended the agreements to provide maturities of March 31, 1980 in the amount of $12,000,000 for Hesston Corporation and $6,218,000 for HCL. The agreements also require that a 1/2% commitment fee be paid on the unused portions of these lines of credit. Borrowings outside the U.S. and Canada are under informal lines of credit with local banks. These lines are normally in the national currency and can be withdrawn at the option of the banks.

The Company and HCL have informally agreed to maintain unrestricted average compensating balances with respect to lines of credit under the Revolving Credit Agreement. At December 31, 1978, the combined compensating balance requirements of the Company and HCL were 10% of lines of credit aggregating $16,975,000. The Company is not required to maintain compensating balances based on usage. Financial statement cash balances are not significantly affected by the compensating balance agreements because these requirements are substantially satisfied by normal float (the time lag in presentation of Hesston checks for payment).

Notes to Consolidated Financial Statements (continued)

5. Short-term bank borrowings (continued)

The following information relates to short-term bank borrowing for the respective periods.

(000's Omitted)

	Three months ended December 31, 1978		Year ended September 30, 1978		Year ended September 30, 1977	
	Hesston Corporation	Hesston Credit, Ltd.	Hesston Corporation	Hesston Credit, Ltd.	Hesston Corporation	Hesston Credit, Ltd.
At the balance sheet date:						
Lines of credit:						
Revolving credit agreement	$14,975	$ 6,218	$14,975	$ 7,723	$14,975	$ 9,856
Open credit lines	21,409		23,363		23,778	
	$36,384	$ 6,218	$38,338	$ 7,723	$38,753	$ 9,856
Short-term loans:						
Revolving credit agreement	$ 6,200	$ 4,318		$ 3,768		$ 233
Other	12,806		$13,131		$14,613	
Weighted average interest rate	11.3%	13.1%	11.0%	11.4%	11.9%	9.8%
For the period ended at the balance sheet date:						
Maximum short-term borrowings outstanding at any month end	$19,006	$ 4,318	$23,530	$ 7,346	$35,030	$10,949
Average borrowings outstanding	$15,359	$ 3,891	$16,400	$ 5,279	$26,475	$ 4,818
Weighted average interest rate	11.1%	12.4%	10.7%	10.3%	10.4%	8.3%

6. Long-term debt and restrictions

Long-term debt, including current maturities, is as follows:

(000's Omitted)

	December 31, 1978	September 30, 1978	September 30, 1977
10.75% promissory notes to insurance company, with annual payments of $2,700,000	$29,600	$29,600	$32,300
Unsecured notes payable to U.S. banks, under Revolving Credit Agreement bearing interest at the prime rate, plus 1/2%, with quarterly payments of $312,000			4,062

6. Long-term debt and restrictions (continued)

	December 31, 1978	September 30, 1978	September 30, 1977
	(000's Omitted)		
9.75% promissory note to Fiat Finance Corp. B.V. due July 31, 1982	3,000	3,000	
Obligations under capital leases, 7%-14%, payable in varying amounts to 1995	2,174	2,202	2,526
Other, 9%-10.3%, payable in varying annual amounts to 1989	3,036	3,578	3,723
	37,810	38,380	42,611
Portion due within one year	(3,343)	(3,223)	(4,633)
	$ 34,467	$35,157	$37,978

In September 1978, the Company borrowed $3,000,000 from Fiat Finance Corp. B.V. The proceeds of the borrowing were used to prepay the Revolving Credit Term Note in the amount of $3,125,000.

The Company's loan agreement with the insurance company and the Revolving Credit Agreement with a number of banks (Note 5) contain restrictions and covenants relating to, among other things, payment of cash dividends, maintenance of working capital and net worth, additional borrowing and acquisition of outstanding stock by the Company. These agreements permit payment of cash dividends on the $1.60 and $.60 Preferred Stock prior to October 1, 1982, provided tangible net worth (as defined) exceeds $42,500,000. At December 31, 1978, tangible net worth was $49,305,000. Cash dividends on common stock are permitted prior to October 1, 1982, provided that tangible net worth exceeds $48,000,000 and net income for the period beginning October 1 in the fiscal year of the first common dividend payment exceeds cash dividends on all preferred and common stock for the period. Subsequent to October 1, 1982, cash dividends on common and preferred stock are subject to certain tests of cumulative net income or loss.

Long-term debt maturing in each of the next five fiscal years is: 1979 - $3,343,000, 1980 - $3,220,000, 1981 - $3,336,000, 1982 - $6,157,000, 1983 - $3,129,000.

7. Income taxes

No provision for income taxes was reported for the three months ended December 31, 1978, since the Company's operations resulted in a loss for both tax and financial reporting purposes and loss carryback benefits were not available. The components of income tax expense (benefit) for the years ended September 30, 1978 and 1977 are:

Hesston Corporation stockholder report

Notes to Consolidated Financial Statements (continued)

7. Income taxes (continued)

	(000's Omitted) 1978	1977
Current:		
Federal	$(4,343)	$(6,739)
State and other	(256)	(604)
	(4,599)	(7,343)
Deferred:		
Federal	957	(539)
State and other	131	(74)
	1,088	(613)
Foreign tax effect of loss carryforwards	878	
Total income tax benefit	$(2,633)	$(7,956)

Other current assets include deferred tax benefits of $2,704,000, $2,704,000, and $4,161,000 at December 31, 1978 and September 30, 1978 and 1977 respectively. Deferred tax expense (benefit) results from differences in the timing of recognizing certain revenues and expenses for income tax and financial statement purposes. The sources of these differences in the periods reported and the tax effect of each were as follows:

	(000's Omitted) Years ended September 30, 1978	1977
Provision for estimated field fix and bad debts	$ 402	$ 21
Provision for discontinued operations	99	467
Excess of tax depreciation over book depreciation	102	271
Sales discounts and allowances in excess of amounts currently deductible	(116)	(476)
Provision for inventory write-downs less than (in excess of) amounts currently deductible	637	(482)
Tax over book gain from sale of fixed assets	(13)	(188)
Other	(23)	(226)
	$ 1,088	$ (613)

Total tax benefit amounted to $2,633,000 (an effective rate of 36.3%) for fiscal 1978 and $7,956,000 (an effective rate of 46.1%) for fiscal 1977, which is less than the $3,482,000 and

7. Income taxes (continued)

$8,290,000 respectively, computed by applying the federal income tax rate of 48% to loss before income taxes. The reasons for these differences are as follows:

	Years ended September 30,	
	1978	1977
Expected federal income tax rate	(48.0)%	(48.0)%
U.S. benefit of asset writeoffs relating to the closing of foreign sales operations	(17.0)	
Operating losses for which no income tax benefit has been recognized	27.0	7.8
Other	1.7	(5.9)
	(36.3)%	(46.1)%

At December 31, 1978, tax operating losses of approximately $2,697,000 are available for indefinite carryforward to offset future taxable income. In addition, approximately $3,407,000 of expenses recorded for financial reporting purposes, for which tax benefits have not been recognized, will be deductible for income tax purposes in future years. For the year ended September 30, 1978, tax benefits in the amount of $878,000 resulting from utilization of a portion of the operating loss carryforwards are reported as an extraordinary item.

8. Preferred stock

The Company has outstanding 600,000 shares of voting $.60 Cumulative Convertible Preferred Stock, par value $2.00. Dividends did not begin to accrue on these shares until March 15, 1978, 180 days after the date of original issue. This class of preferred stock is convertible into common stock on a one-for-one basis and is redeemable on and after September 15, 1982 at $10 per share, plus in each case, accrued dividends to the date of redemption.

The Company also has outstanding 499,800 shares of non-voting $1.60 Cumulative Convertible Preferred Stock, par value $2.00. This class of preferred stock is convertible into common stock at the rate of 1.025 shares of common stock for each share of preferred stock. The preferred stock is redeemable all or in part at the option of the Company at $26.50 per share until 1980 and at prices declining at the rate of $.25 per year through 1985 and thereafter at $25.00 per share, plus in each case, accrued dividends to the date of redemption.

The Company may not acquire shares of preferred stock or common stock, or pay dividends on common stock, unless all dividends on preferred stock for all past dividend periods have been paid or set apart for payment (also see Note 6).

9. Stock option plans

In January 1977, a stock option plan was approved by the stockholders. The maximum number of shares of common stock which may be issued and sold under the plan is 100,000. The option price for such shares will be fair market value at date of grant. Options may be exercised for 20% of

Notes to Consolidated Financial Statements (continued)

9. Stock option plans (continued)

the total grant at the end of the first through the fifth years of the options, such rights being cumulative and expiring ten years after date of grant. On March 30, 1977, options to purchase 72,500 shares of common stock were granted at an option price of $8.25 per share. None of the options granted in 1977 have been exercised at December 31, 1978.

10. Retirement and bonus plans

The Company and its subsidiaries have in effect several trusteed retirement profit-sharing plans, a deferred compensation plan and a cash bonus profit-sharing plan. The profit-sharing plans provide for annual contributions based on percentages of income, some by operating division (as defined by the plans). In January 1979, the Company amended the Cash Bonus and Retirement Plans to provide annual contributions based on a percentage of return on assets. The minimum contribution to the retirement plans as a percent of annual base compensation will be 2% in 1979 and 3% in 1980. The plans may be terminated at any time. Total charges against operations for the retirement plans were $1,051,000 and $872,000 in years ended September 30, 1978 and 1977 respectively, and $247,000 for the three months ended December 31, 1978.

11. Contingencies

Under wholesale finance agreements, the Company has a contingent liability to repurchase equipment sold to dealers. Based on past experience, it is not anticipated that losses under these agreements or other credit losses will be material. Therefore, allowances for losses have not been provided.

The Company is contingently liable for $875,000 of Industrial Revenue Bonds associated with assets previously sold.

12. Research and development

Research and development costs of approximately $845,000 for the three months ended December 31, 1978 and $3,807,000 and $4,028,000 for the years ended September 30, 1978 and 1977 respectively, were charged to operations.

13. Leases

Assets under capital leases included in property, plant and equipment and other assets are as follows:

	(000's Omitted) December 31, 1978	September 30, 1978	September 30, 1977
Land and buildings	$2,208	$2,208	$2,208
Machinery and equipment	550	550	208
Transportation equipment			800
	2,758	2,758	3,216
Less accumulated amortization	329	320	397
	$2,429	$2,438	$2,819

13. Leases (continued)

Future minimum lease payments under capital leases together with the present value of the net minimum lease payments as of December 31, 1978 are as follows:

Year ending December 31,	(000's Omitted)
1979	$ 305
1980	332
1981	313
1982	199
1983	199
Later years	2,419
Total minimum lease payments	3,767
Less amount representing interest	1,593
Present value of minimum lease payments	$2,174

Future minimum rental payments required under operating leases that have initial or remaining non-cancelable lease terms in excess of one year at December 31, 1978 are as follows:

	(000's Omitted)		
Year ending December 31,	Land and Buildings	Machinery and Equipment	Total
1979	$ 542	$ 846	$1,388
1980	436	756	1,192
1981	391	289	680
1982	248	103	351
1983	182	65	247
Later years	221	71	292
	$2,020	$2,130	$4,150

Rents charged to costs and expenses for all operating leases were approximately $560,000 for the three months ended December 31, 1978 and $2,310,000 and $2,926,000 for the years ended September 30, 1978 and 1977 respectively.

14. Foreign operations and segment information

The Company is engaged principally in the design, manufacture and sale of farm equipment through a worldwide organization. Information about the Company's operations in different

Hesston Corporation stockholder report

Notes to Consolidated Financial Statements (continued)

14. Foreign operations and segment information (continued)

geographic areas is summarized below (000's omitted):

At September 30, 1978 and for the year then ended:

	United States	Europe	Canada & Australia	Eliminations	Consolidated
Trade sales	$125,723	$30,892	$ 9,381		$165,996
Interarea sales	8,617	521		$(9,138)	
Total revenue	$134,340	$31,413	$ 9,381	$(9,138)	$165,996
Income (loss) before income taxes and extraordinary item	$ (5,968)	$ 567	$(1,810)	$ (44)	$ (7,255)
Identifiable assets	$ 92,201	$32,096	$ 6,568	$(6,005)	$124,860
Corporate assets					15,999
Total assets					$140,859

At December 31, 1978 and for the three months then ended:

	United States	Europe	Canada & Australia	Eliminations	Consolidated
Trade sales	$30,174	$ 7,507	$1,711		$ 39,392
Interarea sales	1,854	51		$(1,905)	
Total revenue	$32,028	$ 7,558	$1,711	$(1,905)	$ 39,392
Income (loss) before income taxes and extraordinary item	$ (2,896)	$ 343	$ (72)	$ (276)	$ (2,901)
Identifiable assets	$91,922	$31,898	$4,047	$(2,038)	$ 125,829
Corporate assets					17,757
Total assets					$ 143,586

Interarea sales are accounted for on a basis designed to allow both the purchaser and supplier a fair return on assets under normal operating conditions.

Identifiable assets are those identified with the operations in each geographic area. Corporate assets consist mainly of an office building, communications center and refundable income taxes.

United States trade sales include $917,000 for the three months ended December 31, 1978 and $5,581,000 for the year ended September 30, 1978 to unaffiliated foreign customers, principally in Canada, Europe and Latin America.

Other expenses in the consolidated statements include exchange losses of $16,000 for the three months ended December 31, 1978 and $1,672,000 and $465,000 for the years ended September 30, 1978 and 1977 respectively. Other expenses also include $959,000 in the year ended September 30, 1978 for closing the Australian sales subsidiary.

15. Related party transactions

In August 1978, the Company closed its sales operations in Australia. Fiat of Australia Pty. Ltd. was appointed as distributor of the Company's products in Australia and most of the Company's inventories in Australia were sold to Fiat of Australia. The Company received $2,011,000 in cash and an account receivable, which approximated the book value of the inventories sold.

During the three month period ended December 31, 1978, the Company's manufacturing facility at Udine, Italy, was sold to Fiat Trattori S.p.A. for approximately $360,000, which exceeded book value. Products previously manufactured at this facility are now manufactured at the Company's facility in Coex, France.

In September 1978, the Company borrowed $3,000,000 from Fiat Finance Corp. B.V. (Note 6).

16. Replacement cost information (Unaudited)

In compliance with the rules of the Securities and Exchange Commission (SEC), the Company has developed certain replacement cost information, as defined by the SEC, for its worldwide inventories, cost of sales and productive capacity which is included in the Company's Annual Report Form 10-K. The information indicates that replacement costs and related depreciation expense would be considerably higher than the historical amounts contained in the financial statements. Such data was derived based on numerous subjective and hypothetical assumptions. The Company has no intention of replacing any significant amount of these assets at this time and cautions that the actual cost and manner of replacing these assets in the future may differ substantially from these estimates.

The replacement cost data does not purport to represent the current value of the assets, and the Company makes no representation that this information is useful to the reader of these financial statements.

ARTHUR YOUNG & COMPANY

TEN MAIN CENTER
KANSAS CITY, MISSOURI 64105

The Board of Directors and Stockholders
Hesston Corporation

We have examined the accompanying consolidated balance sheets of Hesston Corporation at December 31, 1978 and September 30, 1978 and 1977, and the related consolidated statements of operations, stockholders' equity and changes in financial position for the three month period ended December 31, 1978 and the fiscal years ended September 30, 1978 and 1977. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the statements mentioned above present fairly the consolidated financial position of Hesston Corporation at December 31, 1978 and September 30, 1978 and 1977, and the consolidated results of operations and changes in financial position for the three month period ended December 31, 1978 and the fiscal years ended September 30, 1978 and 1977, in conformity with generally accepted accounting principles applied on a consistent basis during the period.

Arthur Young & Company

February 20, 1979

Directors

Paolo Bernardelli
Director of Marketing of Fiat Trattori S.p.A.

Howard L. Brenneman*
President and Chief Operating Officer of the Corporation

Stefano Decio*
Special Assistant to General Manager of Fiat Trattori S.p.A.

Harold P. Dyck
Consultant for the Mennonite Foundation, Inc. - Investments

Richard F. Hrdlicka
Senior Vice President - General Counsel and Secretary of the Corporation

Fernando Negro
Consultant to Fiat S.p.A.

Jonathan O'Herron
General Partner Lazard Freres & Co., investment bankers

Pietro Quaglia*
Vice President of Fiat U.S. Representative, Inc.

Piero Bondesan*
Corporate Controller for Agricultural Tractor and Construction Machinery activities of Fiat

Melvin H. Voth
Vice President - Finance, Treasurer & Assistant Secretary of the Corporation

Lyle E. Yost*
Chairman of the Board and Chief Executive Officer of the Corporation

*Members of Executive Committee

Officers

Lyle E. Yost
Chairman - Chief Executive Officer

Howard L. Brenneman
President - Chief Operating Officer

Raymond C. Schlichting
Senior Vice President

Richard F. Hrdlicka
Senior Vice President - General Counsel and Secretary of the Corporation

Raymond A. Adee
Vice President - Product Planning Hesston Division

Max E. Bennett
Vice President - General Manager, Hesston Division

John Siemens, Jr.
Vice President - Administration

Melvin H. Voth
Vice President - Finance, Treasurer & Assistant Secretary

Carl D. Wohlgemuth
Vice President - Planning

Samuel W. White, Jr.
Vice President - Business Affairs

Donald L. Schmidt
Corporate Controller

Robert D. Taylor
Assistant Treasurer

Transfer Agents

The Chase Manhattan Bank, N.A., New York, New York
The Fourth National Bank & Trust Company, Wichita, Kansas

Registrars

The Chase Manhattan Bank, N.A., New York, New York
The First National Bank in Wichita, Wichita, Kansas