

ARTS WAY MANUFACTURING CO INC  
Form 10QSB  
October 07, 2008

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

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FORM 10-QSB

(Mark One)

Quarterly report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934  
For the quarterly period ended August 31, 2008

Transition report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File No. 0-5131

ART'S-WAY MANUFACTURING CO., INC.  
(Exact Name of Small Business Issuer as Specified in Its Charter)

DELAWARE  
(State or Other Jurisdiction of Incorporation or  
Organization)

42-0920725  
I.R.S. Employer Identification No.

5556 Highway 9, Armstrong, Iowa  
50514  
(Address of Principal Executive Offices)

(712) 864-3131  
Issuer's Telephone Number, Including Area Code

Check whether the issuer (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Exchange Act during the past 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  No

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

Number of common shares outstanding as of September 11, 2008: 3,974,352

Transitional Small Business Disclosure Format (check one): Yes  No

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**ART'S-WAY MANUFACTURING CO., INC.**  
Consolidated Balance Sheets

	(Unaudited)	
	August 2008	November 2007
<b>Assets</b>		
Current assets:		
Cash	\$ 295,066	\$ 612,201
Accounts receivable-customers, net of allowance for doubtful accounts of \$225,286 and \$148,636 in 2008 and 2007, respectively	3,247,616	3,087,781
Inventories, net	14,044,011	8,636,602
Deferred taxes	850,000	773,555
Cost and Profit in Excess of Billings	582,221	265,615
Other current assets	243,799	408,870
Total current assets	19,262,713	13,784,624
Property, plant, and equipment, net	6,689,044	5,497,200
Covenant not to Compete	255,000	300,000
Goodwill	375,000	375,000
Other Assets	8,308	9,771
Total assets	\$ 26,590,065	\$ 19,966,595
<b>Liabilities and Stockholders' Equity</b>		
Current liabilities:		
Notes payable to bank	\$ 2,151,943	\$ 397,859
Current portion of term debt	421,602	250,027
Accounts payable	2,830,874	1,368,988
Customer deposits	441,463	53,196
Billings in Excess of Cost and Profit	407,394	7,675
Accrued expenses	1,430,493	1,323,008
Income taxes payable	47,500	146,905
Total current liabilities	7,731,269	3,547,658
Long-term liabilities		
Deferred taxes	430,000	205,998
Term debt, excluding current portion	6,190,627	6,069,657
Total liabilities	14,351,896	9,823,313
Stockholders' equity:		
Common stock – \$0.005 par value. Authorized 5,000,000 shares; issued 3,974,352 and 3,968,352 shares in 2008 and 2007	19,872	19,842
Additional paid-in capital	2,019,010	1,828,427
Retained earnings	10,199,287	8,295,013
Total stockholders' equity	12,238,169	10,143,282
Total liabilities and stockholders' equity	\$ 26,590,065	\$ 19,966,595

See accompanying notes to consolidated financial statements.

**ART'S-WAY MANUFACTURING CO., INC.**

## Consolidated Statements of Operations

## Condensed

	Three Months Ended		Year to Date	
	August 31, 2008	August 31, 2007	August 31, 2008	August 31, 2007
Net sales	\$ 9,420,696	\$ 8,191,523	\$ 23,855,763	\$ 19,165,728
Cost of goods sold	7,214,281	5,410,688	17,035,449	13,201,569
Gross profit	2,206,415	2,780,835	6,820,314	5,964,159
Expenses:				
Engineering	110,031	59,401	259,707	273,510
Selling	495,658	297,522	1,373,388	750,573
General and administrative	730,242	575,348	2,463,615	1,846,250
Total expenses	1,335,931	932,271	4,096,710	2,870,333
Income from operations	870,484	1,848,564	2,723,604	3,093,826
Other income (expense):				
Interest expense	(133,164)	(154,440)	(399,453)	(332,651)
Other	69,992	(177,309)	505,706	176,644
Total other income	(63,172)	(331,749)	106,253	(156,007)
Income before income taxes	807,312	1,516,815	2,829,857	2,937,819
Income tax	268,923	586,767	925,582	1,069,312
Net income	\$ 538,389	\$ 930,048	\$ 1,904,275	\$ 1,868,507
Net income per share:				
Basic	0.14	0.24	0.48	0.47
Diluted	0.13	0.23	0.48	0.47

See accompanying notes to consolidated financial statements.

**ART'S-WAY MANUFACTURING CO., INC.**

## Consolidated Statements of Cash Flows

## Condensed

	Year To Date	
	August 2008	August 2007
<b>Cash flows from operations:</b>		
Net income	\$ 1,904,275	\$ 1,868,507
<b>Adjustments to reconcile net income to net cash provided (used) by operating activities:</b>		
Stock based compensation	145,851	42,766
(Gain) Loss on disposal of property, plant, and equipment	(418,269)	(329,258)
Depreciation expense	392,233	244,112
Amortization expense	45,000	-
Fire loss of operating supplies	-	(364,409)
Deferred income taxes	147,557	155,349
<b>Changes in assets and liabilities:</b>		
<b>(Increase) decrease in:</b>		
Accounts receivable	(159,835)	(421,627)
Inventories	(5,407,409)	(1,561,847)
Other current assets	(83,801)	(30,602)
Other, net	1,464	110,240
<b>Increase (decrease) in:</b>		
Accounts payable	1,461,886	280,335
Contracts in progress, net	83,113	(223,590)
Customer deposits	388,267	(141,653)
Income taxes payable	(99,405)	13,181
Accrued expenses	107,485	199,318
Net cash (used in) operating activities	(1,491,588)	(159,178)
<b>Cash flows from investing activities:</b>		
Purchases of property, plant, and equipment	(1,584,079)	(1,269,618)
Proceeds from insurance recoveries	666,591	1,233,633
Proceeds from sale of property, plant, and equipment	550	-
Net cash (used in) investing activities	(916,938)	(35,985)
<b>Cash flows from financing activities:</b>		
Net change in line of credit	1,754,084	390,531
Payments of notes payable to bank	(207,455)	(27,185)
Proceeds from term debt	500,000	-
Proceeds from the exercise of stock options	44,762	-
Net cash provided by financing activities	2,091,391	363,346
Net increase (decrease) in cash	(317,135)	168,183
Cash at beginning of period	612,201	2,072,121
Cash at end of period	\$ 295,066	\$ 2,240,304
<b>Supplemental disclosures of cash flow information:</b>		
<b>Cash paid/(received) during the period for:</b>		
Interest	\$ 366,821	\$ 330,534
Income taxes	877,380	863,129

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<b>Supplemental disclosures of noncash investing activities:</b>			
Proceeds from insurance recoveries	\$	666,591	\$ 1,233,633
Insurance recoveries receivable		-	248,872
Gains recognized in previous years		(248,872)	
<b>Net book value of assets destroyed</b>			
Property, plant and equipment		-	(339,258)
Cost incurred on contracts in progress		-	(379,375)
Cost incurred for plant supplies			(364,409)
Inventories		-	(70,205)
Gain on insurance recovery	\$	417,719	\$ 329,258
<b>Non cash financing activity:</b>			
Refinanced existing debt with West Bank			\$ 4,100,000.00

See accompanying notes to consolidated financial statements.

## Notes to Consolidated Financial Statements

### (1) Summary of Significant Account Policies

#### Statement Presentation

The financial statements are unaudited and reflect all adjustments (consisting only of normal recurring adjustments) which are, in the opinion of management, necessary for a fair presentation of the financial position and operating results for the interim periods. The financial statements should be read in conjunction with the financial statements and notes thereto contained in the Company's Annual Report on Form 10-KSB for the year ended November 30, 2007. The results of operations for the nine months ended August 31, 2008 are not necessarily indicative of the results for the fiscal year ending November 30, 2008.

### (2) Income Per Share

Basic net income per common share has been computed on the basis of the weighted average number of common shares outstanding. Diluted net income per share has been computed on the basis of the weighted average number of common shares outstanding plus equivalent shares assuming exercise of stock options.

Basic and diluted earnings per common share have been computed based on the following as of August 31, 2008 and 2007:

	<b>For the three months ended</b>	
	<b>August 31, 2008</b>	<b>August 31, 2007</b>
<b>Basic:</b>		
Numerator, net income	\$ 538,389	\$ 930,048
Denominator: Average number of common shares outstanding	3,972,548	3,956,352
Basic earnings per common share	\$ 0.14	\$ 0.24
<b>Diluted</b>		
Numerator, net income	\$ 538,389	\$ 930,048
Denominator: Average number of common shares outstanding	3,972,548	3,956,352
Effect of dilutive stock options	17,332	19,552
	3,989,880	3,975,904
Diluted earnings per common share	\$ 0.13	\$ 0.23

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	<b>For the nine months ended</b>	
	<b>August 31, 2008</b>	<b>August 31, 2007</b>
<b>Basic:</b>		
Numerator, net income	\$ 1,904,275	\$ 1,868,507
Denominator: Average number of common shares outstanding	3,971,676	3,956,352
Basic earnings per common share	\$ 0.48	\$ 0.47
<b>Diluted</b>		
Numerator, net income	\$ 1,904,275	\$ 1,868,507
Denominator: Average number of common shares outstanding	3,971,676	3,956,352
Effect of dilutive stock options	22,348	10,498
	3,994,024	3,966,850
Diluted earnings per common share	\$ 0.48	\$ 0.47

Shares and per share data have been adjusted to reflect the two for one stock split effective July 30, 2008.

### (3) Inventories

Major classes of inventory are:

	<b>August 31, 2008</b>	<b>November 30, 2007</b>
Raw materials	\$ 9,505,292	\$ 4,468,920
Work in process	1,378,488	336,108
Finished goods	4,777,655	5,033,063
	\$ 15,661,435	\$ 9,838,091
Less: Reserves	(1,617,424)	(1,201,489)
	\$ 14,044,011	\$ 8,636,602

### (4) Accrued Expenses

Major components of accrued expenses are:

	<b>August 31, 2008</b>	<b>November 30, 2007</b>
Salaries, wages, and commissions	\$ 868,757	\$ 562,806
Accrued warranty expense	324,415	262,665
Other	237,321	497,537
	\$ 1,430,493	\$ 1,323,008

**(5) Product Warranty**

The Company offers warranties of various lengths to its customers depending on the specific product and terms of the customer purchase agreement. The average length of the warranty period is 1 year from the date of purchase. The Company's warranties require it to repair or replace defective products during the warranty period at no cost to the customer. The Company records a liability for estimated costs that may be incurred under its warranties. The costs are estimated based on historical experience and any specific warranty issues that have been identified. Although historical warranty costs have been within expectations, there can be no assurance that future warranty costs will not exceed historical amounts. The Company periodically assesses the adequacy of its recorded warranty liability and adjusts the balance as necessary.

Changes in the Company's product warranty liability for the three and nine months ended August 31, 2008 and August 31, 2007 are as follows:

	<b>Three Months Ended</b>	
	<b>August 31, 2008</b>	<b>August 31, 2007</b>
Balance, beginning	\$ 240,141	\$ 253,853
Settlements made in cash or in-kind	(2,059)	58,112
Warranties issued	86,333	50,566
Balance, ending	\$ 324,415	\$ 362,531

	<b>Nine Months Ended</b>	
	<b>August 31, 2008</b>	<b>August 31, 2007</b>
Balance, beginning	\$ 262,665	\$ 230,740
Settlements made in cash or in-kind	(264,537)	(60,707)
Warranties issued	326,287	192,498
Balance, ending	\$ 324,415	\$ 362,531

**(6) Loan and Credit Agreements**

The Company has a revolving line of credit for \$3,500,000 that matures on April 30, 2009, with advances funding the working capital, letter of credit and corporate credit card needs. The interest rate is West Bank's prime interest rate, adjusted daily. As of August 31, 2008, the interest rate was 5.0%. Monthly interest only payments are required and the unpaid principal is due on the maturity date. Collateral consists of a first position on assets owned by the Company including, but not limited to inventories, accounts receivable, machinery and equipment. As of August 31, 2008 and November 30, 2007, the Company had borrowed \$2,151,943 and \$397,859 respectively, against the line of credit. The available amounts remaining on the line of credit were \$1,348,057 and \$3,102,141 on August 31, 2008 and November 30, 2007, respectively. Other terms and conditions of the debt with West Bank include providing monthly internally prepared financial reports including accounts receivable aging schedules and borrowing base certificates and year-end audited financial statements. The borrowing base shall limit advances from line of credit to 60% of accounts receivable less than 90 days, 60% of finished goods inventory, 50% of raw material inventory and 50% of work-in-process inventory plus 40% of appraisal value of machinery and equipment.



On June 7, 2007 the Company restructured its long-term debt with West Bank. The Company now has one loan for \$4,100,000. The loan was written to mature on May 1, 2017 and bore interest at the U.S. daily 5-year treasury index plus 2.75 bps fixed for 5 years and was set to adjust to the prevailing same index and margin on the fifth anniversary of the loan for the balance of the term. On May 1, 2008, the terms of this loan were changed to modify the maturity date, interest rate, and payments. The loan, with a principal amount of \$3,898,161, will now mature on May 1, 2013 and bears interest at 5.75%. Monthly principal and interest payments in the amount of \$42,500 are required, with a final payment of principal and accrued interest in the amount of \$2,304,789 due on May 1, 2013.

The Company obtained two additional loans in 2007. Both of these loans were to finance the construction of the new facilities in Monona and Dubuque. On October 9, 2007, the Company obtained a loan for \$1,330,000 that bore interest at the U.S. daily 5-year treasury index plus 2.75 bps, fixed at 7% for 5 years and then adjusted to the prevailing same index and margin on the fifth anniversary for the balance of the term. On May 1, 2008 the terms of this loan were changed to modify the maturity date, interest rate, and payments. On May 1, 2008, the principal amount of the loan was \$1,316,003. The new terms changed the maturity date to May 1, 2013 and the interest rate is now 5.75%. Monthly payments of \$11,000 are required for principal and interest, with a final payment of accrued interest and principal in the amount of \$1,007,294 due on May 1, 2013.

On November 30, 2007, the Company obtained a construction loan to finance the Dubuque, Iowa facility. This loan has a principal amount of \$1,500,000. The loan bore interest at the U.S. daily 5-year treasury index plus 2.75 bps, fixed at 7.25% for 5 years and then was written to adjust to the prevailing same index and margin on the fifth anniversary for the balance of the term. On December 19, 2007, the additional \$500,000 available was disbursed. On May 1, 2008 the terms of this loan were changed to modify the maturity date, interest rate, and payments. On May 1, 2008, the principal amount of the loan was \$1,498,063. The new terms changed the maturity date to May 1, 2013 and the interest rate is now 5.75%. Payments of \$12,550 are due monthly for principal and interest, with a final accrued interest and principal payment in the amount of \$1,114,714 due on May 1, 2013.

Prior to the refinancing discussed above, J. Ward McConnell, Jr. was required to personally guarantee the debt on the old loans with West Bank on an unlimited and unconditional basis. The Company compensated Mr. McConnell for his personal guarantee at an annual percentage rate of 2% of the outstanding balance to be paid monthly. Guarantee fee payments to Mr. McConnell were approximately \$30,000 for the nine months ended August 31, 2007.

A summary of the Company's term debt is as follows:

	<b>August 31, 2008</b>	<b>November 30, 2007</b>
West Bank loan payable in monthly installments of \$42,500 including interest at 5.75% due May 1, 2013 (A)	3,827,603	3,989,684
West Bank loan payable in monthly installments of \$11,000 including interest at 5.75% due May 1, 2013(A)	1,302,275	1,330,000
West Bank loan payable in monthly installments of \$12,550 including interest at 5.75% due May 1, 2013 (A)	1,482,351	1,000,000
<b>Total term debt</b>	<b>6,612,229</b>	<b>6,319,684</b>
<b>Less current portion of term debt</b>	<b>421,602</b>	<b>250,027</b>
<b>Term debt, excluding current portion</b>	<b>\$ 6,190,627</b>	<b>\$ 6,069,657</b>



(A) Covenants include, but are not limited to, debt service coverage ratio and debt/tangible net worth ratio. These loans are secured by real estate and an unlimited guarantee of Art's-Way Vessels, Inc. and Art's-Way Scientific, Inc.

The Company was in compliance with all debt covenants as of August 31, 2008.

#### **(7) Recently Issued Accounting Pronouncements**

In June 2006, the FASB issued Financial Interpretation No. 48, Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109 (Issued 6/06). This Interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. It also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. For the Company, the Statement is effective for fiscal years beginning after December 15, 2006. The adoption of FIN 48 has not had any material impact on the Company's financial position, results of operations, or cash flows.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. This statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosure about fair value measurements. The statement does not require any new fair value measurements, but for some entities, the application of the statement will change current practice. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. FASB Staff Position FAS 157-1 and FAS 157-2 were issued in February 2008. FSP FAS 157-1 amends SFAS No. 157 to exclude pronouncements that address the fair value measurement for lease classifications from the scope of SFAS No. 157. FSP FAS 157-2 delays the effective date of SFAS No. 157 to fiscal years beginning after November 15, 2008. This delay does not include items that are recognized or disclosed at fair value in the financial statements on a recurring basis. The applicable elements of FAS 157 that are currently effective have been adopted by the Company without a material impact on the financial statements. The elements of FAS 157 that are not yet effective are not expected to have a material impact on the financial statements.

In December 2007, the FASB issued FASB Statement No. 141 (Revised 2007) "Business Combinations," which requires the Company to record fair value estimates of contingent consideration and certain other potential liabilities during the original purchase price allocation, expense acquisition costs as incurred and does not permit certain restructuring activities previously allowed to be recorded as a component of purchase accounting. SFAS No. 141(R) applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008, except for the presentation and disclosure requirements, which shall be applied retrospectively for all periods presented. The Company has not determined the effect that the adoption of SFAS No. 141(R) will have on the financial results of the Company.

In December 2007, the FASB issued FASB Statement No. 160 "Noncontrolling Interests in Consolidated Financial Statements – an amendment of ARB No. 51," which causes noncontrolling interests in subsidiaries to be included in the equity section of the balance sheet. SFAS No. 160 applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008, except for the presentation and disclosure requirements, which shall be applied retrospectively for all periods presented. The Company has not determined the effect that the adoptions of SFAS No. 160 will have on the financial results of the Company.

In December 2007, the SEC published SAB 110, *Share-Based Payment*. The interpretations in SAB 110 express the SEC staff's views regarding the acceptability of the use of a "simplified" method, as discussed in SAB 107, in developing an estimate of expected term of share options in accordance with FASB Statement No. 123 (Revised) *Share-Based Payment*. The use of the simplified method requires our option plan to be consistent with a "plain

vanilla" plan and was originally permitted through December 31, 2007 under SAB 107. In December 2007, the SEC issued SAB 110, *Share-Based Payment*, to amend the SEC's views discussed in SAB 107 regarding the use of the simplified method in developing an estimate of expected life of share options in accordance with FAS No. 123(R). SAB 110 is effective for the Company beginning December 31, 2007. The Company will continue to use the simplified method until it has the historical data necessary to provide a reasonable estimate of expected life, in accordance with SAB 107, as amended by SAB 110.

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In February 2007, the FASB issued SFAS No. 159, the Fair Value Option for Financial Assets and Financial Liabilities. SFAS 159 provides entities with an option to report selected financial assets and liabilities at fair value and establishes presentation and disclosure requirements designed to facilitate comparisons between companies that select different measurement attributes. SFAS 159 is effective for fiscal years beginning after November 15, 2007. SFAS No. 159 has been adopted by the Company, and has had no material impact on its financial statements.

#### **(8) Stock Option Plan**

On January 25, 2007 the Board of Directors adopted the 2007 Non-Employee Directors' Stock Option Plan, which was approved by the stockholders at the Annual Stockholders' Meeting on April 24, 2008. Options will be granted to non-employee directors to purchase shares of common stock of the Company at a price not less than fair market value at the date the options are granted. Non-employee directors are automatically granted options to purchase 2,000 shares of common stock annually or initially upon their election to the Board, which are automatically vested. Options granted are nonqualified stock options.

On February 5, 2007 the Board of Directors adopted the 2007 Employee Stock Option Plan which was approved by the stockholders at the Annual Stockholders' Meeting on April 26, 2007.

#### **(9) 2007 Acquisition**

Effective September 5, 2007, the Company acquired the product lines of Miller Pro, Victor and Badger from Miller-St. Nazianz, Inc. for a cash purchase price of approximately \$2,338,000. The operating results of the acquired business are reflected in the Company's consolidated statement of operations from the acquisition date forward. The acquisition was made to continue the Company's growth strategy and diversify its product offerings inside the agricultural industry. The purchase price was determined based on an arms-length negotiated value. The transaction was accounted for under the purchase method of accounting, with the purchase price allocated to the individual assets acquired.

#### **(10) Segment Information**

There are three reportable segments: agricultural products, pressurized vessels and modular buildings. The agricultural products segment fabricates and sells farming products as well as replacement parts for these products in the United States and worldwide. The pressurized vessel segment produces pressurized tanks. The modular building segment produces modular buildings for animal containment and various laboratory uses.

The accounting policies applied to determine the segment information are the same as those described in the summary of significant accounting policies. Management evaluates the performance of each segment based on profit or loss from operations before income taxes, exclusive of nonrecurring gains and losses.

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Approximate financial information with respect to the reportable segments is as follows.

	Three Months Ended August 31, 2008			
	Agricultural Products	Pressurized Vessels	Modular Buildings	Consolidated
Revenue from external customers	\$ 6,685,000	\$ 25,000	\$ 2,711,000	\$ 9,421,000
Income from operations	580,000	(241,000)	531,000	870,000
Income before tax	546,000	(279,000)	540,000	807,000
Total Assets	19,274,000	2,643,000	4,673,000	26,590,000
Capital expenditures	327,000	41,000	56,000	424,000
Depreciation & Amortization	118,000	13,000	24,000	155,000

	Three Months Ended August 31, 2007			
	Agricultural Products	Pressurized Vessels	Modular Buildings	Consolidated
Revenue from external customers	\$ 4,552,000	\$ 1,319,000	\$ 2,321,000	\$ 8,192,000
Income from operations	943,000	286,000	620,000	1,849,000
Income before tax	679,000	266,000	572,000	1,517,000
Total Assets	11,956,000	2,094,000	3,596,000	17,646,000
Capital expenditures	34,000	55,000	1,017,000	1,106,000
Depreciation & Amortization	60,000	14,000	0	74,000

	Nine Months Ended August 31, 2008			
	Agricultural Products	Pressurized Vessels	Modular Buildings	Consolidated
Revenue from external customers	\$ 15,878,000	\$ 228,000	\$ 7,750,000	\$ 23,856,000
Income from operations	1,872,000	(701,000)	1,553,000	2,724,000
Income before tax	1,744,000	(815,000)	1,901,000	2,830,000
Total Assets	19,274,000	2,643,000	4,673,000	26,590,000
Capital expenditures	659,000	751,000	175,000	1,585,000
Depreciation & Amortization	338,000	34,000	65,000	437,000

	Nine Months Ended August 31, 2007			
	Agricultural Products	Pressurized Vessels	Modular Buildings	Consolidated
Revenue from external customers	\$ 10,927,000	\$ 3,573,000	\$ 4,666,000	\$ 19,166,000
Income from operations	1,329,000	816,000	949,000	3,094,000
Income before tax	1,008,000	752,000	1,178,000	2,938,000
Total Assets	11,956,000	2,094,000	3,596,000	17,646,000
Capital expenditures	150,000	72,000	1,048,000	1,270,000
Depreciation & Amortization	189,000	39,000	16,000	244,000

**(11) Stock Split**

The Board of Directors announced a two-for-one stock split with a record date of July 23, 2008. The stock began trading on the split-adjusted basis on July 31, 2008. The Board of Directors has also approved a \$0.06 per share dividend for all stockholders of record on November 15, 2008, which will be paid on or before November 30, 2008.

**(12) Subsequent Events**

None.

Item 2

**MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION**

The following discussion and analysis should be read in conjunction with the consolidated financial statements and notes thereto appearing elsewhere in this report. Some of the statements in this report may contain forward-looking statements that reflect our current view on future events, future business, industry and other conditions, our future performance, and our plans and expectations for future operations and actions. In some cases you can identify forward-looking statements by the use of words such as "may," "should," "anticipate," "believe," "expect," "plan," "future," "could," "estimate," "predict," "hope," "potential," "continue," or the negative of these terms or other similar expressions. Many of these forward-looking statements are located in this report under "Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION," but they may appear in other sections as well.

You should read this report thoroughly with the understanding that our actual results may differ materially from those set forth in the forward-looking statements for many reasons, including events beyond our control and assumptions that prove to be inaccurate or unfounded. We cannot provide any assurance with respect to our future performance or results. Our actual results or actions could and likely will differ materially from those anticipated in the forward-looking statements for many reasons, including the reasons described in this report. We are not under any duty to update the forward-looking statements contained in this report. We cannot guarantee future results, levels of activity, performance or achievements. We caution you not to put undue reliance on any forward-looking statements, which speak only as of the date of this report. You should read this report and the documents that we reference in this report and have filed as exhibits completely and with the understanding that our actual future results may be materially different from what we currently expect. We qualify all of our forward-looking statements by these cautionary statements.

(a) **Management's Discussion and Analysis of Financial Condition and Results of Operations**

(i) **Critical Accounting Policies**

Our critical accounting policies involving the more significant judgments and assumptions used in the preparation of the financial statements as of August 31, 2008 have remained unchanged from November 30, 2007. These policies involve revenue recognition, inventory valuation and income taxes. Disclosure of these critical accounting policies is incorporated by reference under Note 1 of the financial statements in our Annual Report on Form 10-KSB for the year ended November 30, 2007.

(ii)

Results of Operations*Net Sales*

Our consolidated net sales for the nine months ended were \$23,856,000, representing a 24.5% increase compared to the same period one year ago. Net sales for the quarter ended August 31, 2008 increased by \$1,229,000 over the same period in 2007, representing a 15.0% increase. The consolidated increase in net sales for the nine month period just ended was due to the increased sales of Art's-Way Scientific, Inc. by 66% and Art's-Way Manufacturing's sales increase of 45.3%. These two increases, however, were offset by Art's-Way Vessels' decrease in net sales of 93.6%. Art's-Way Manufacturing had revenues totaling \$15,878,000 for the nine months just ended, compared to \$10,927,000 for the same period in 2007. The increase in sales for Art's-Way Manufacturing was largely due to the \$3,410,000 year-to-date sales from the Miller Pro product line. Art's-Way Vessels had revenues totaling \$228,000 for the nine months just ended, compared to \$3,573,000 for the same period in 2007. Art's-Way Vessels has hired a general manager, and is currently in the process of hiring additional staff to fulfill anticipated production needs. Our general manager is well known in the industrial water treatment industry, and is very familiar with the types of tanks we manufacture. The process of rebuilding our sales lost during our move to a new facility has taken longer than originally anticipated, but we anticipate that sales will increase in the fourth quarter and throughout 2009 with the general manager's guidance. Art's-Way Vessels is expected to increase production of tanks after completing 80 graders for Art's-Way Manufacturing. Art's-Way Scientific has revenues totaling \$7,750,000 for the nine months just ended, compared to \$4,666,000 for the same period in 2007. On January 16, 2007, Art's-Way Scientific suffered the loss of the Monona manufacturing facility to fire. The growth in revenues at Art's-Way Scientific is primarily due to resuming full operations in our newly constructed manufacturing facility.

Consolidated year-to-date gross profit decreased to 28.6% from 31.1% in 2007. This decrease is due to several different factors. The gross profit for Art's-Way Manufacturing decreased from 35.6% for the third quarter in 2007 to 24.4% for the same period in 2008. While we have been gearing up for full production of the Miller Pro product line, we outsourced many items due to the capacity limitations of our laser cutting machine. We have since purchased a plasma cutter to reduce these expenses. Our manufacturing wage expenses for the quarter were \$938,000 compared to \$675,000 for the same period in 2007. This increase is a result of hiring and training additional staff for our increased production. These factors, along with the rising costs of our inputs, such as steel and freight, have negatively impacted our gross profits. Art's-Way Vessels has a gross profit of -637.7% and 32.7% in the third quarter of 2008 and 2007, respectively. Certain manufacturing expenses, such as depreciation for manufacturing equipment and inventory obsolescence, are consistent despite reduced sales. Also during this time, we had to outsource our engineering work due to the loss of our staff engineer. This position has since been filled. Costs for steel and freight also negatively impact the gross profit of Art's-Way Vessels. Art's-Way Scientific's gross profit for the third quarter of 2008 was 27.2% compared to 31.4%. The combination of these factors has resulted in a consolidated gross profit of 23.4% for the third quarter of 2008, compared to 33.9% for the same period in 2007.

*Expenses*

Consolidated operating expenses for the nine months just ended increased \$1,226,000 compared to 2007. As a percent of sales, operating expenses increased by 2.2% for the nine months just ended, up from 15.0% in 2007 to 17.2% in 2008. Art's-Way Manufacturing's year-to-date operating expenses as a percentage of sales were 19.6%, Art's-Way Vessels' were 148.3% and Art's-Way Scientific's were 8.4%.

General and administrative expenses for the quarter increased \$155,000 as compared to the same period in 2007. Much of this increase is due to the gradual addition of administrative staff. Year-to-date general and administrative expenses as a percentage of sales were 10.3% compared to 9.6% in 2007.



Engineering expenses are down \$14,000 for the nine months ended, but increased by \$51,000 for the three months ended, compared to the same period in 2007. This increase is due to a research and development project that was completed in the third quarter of 2008. As a percentage of sales, year-to-date engineering expenses are down from 1.4% in 2007 to 1.1% in 2008.

Selling expenses are up for the nine months ended by \$623,000 compared to the same period in 2007. As a percentage of sales, year-to-date selling expenses increased from 3.9% in 2007 to 5.8% in 2008. The majority of the increase is due to additional sales staff and trade show expenses for the Miller Pro product line.

Interest expense for the nine months ended increased by \$67,000 due to the addition of a \$1,500,000 loan and a \$1,330,000 loan in the fourth quarter of 2007, and increased borrowings on the line of credit. This increase was partially offset by the reduced interest rates during 2008 compared to 2007.

Other income increased by \$329,000 in the nine months ended August 31, 2008 compared to the same period in 2007. The increase is primarily due to the timing of gains recognized for the fire in Monona in 2007 and 2008, which was included under the caption "Other" on the Consolidated Statement of Operations. The accounting for fire recoveries increased the modular buildings segment and consolidated results by \$417,000 in 2008. Proceeds, and any resulting gain, are recognized in the period in which claim settlements are reached. As of August 31, 2008, portions of the insurance settlement for the fire are still pending.

#### *Order Backlog*

The consolidated order backlog as of September 2008 is \$16,947,000 compared to \$12,453,000 one year ago. Art's-Way Manufacturing's order backlog as of September 2008 is \$8,207,000 compared to \$2,773,000 in 2007. Art's-Way Vessels backlog is \$105,000 in 2008 compared to \$417,000 in 2007. Our lease for our Dubuque facility for Art's-Way Vessels expired on October 4, 2007, and we moved into our newly constructed facility in February 2008. Art's-Way Scientific's backlog is \$8,635,000 as of September 2008 compared to \$9,263,000 in 2007. In 2007, the backlog at Art's-Way Scientific included orders that had been destroyed by fire during production.

#### *Seasonality*

Our beet equipment traditionally is shipped mostly during our third quarter. As of August 31, 2008, four beet harvesters were awaiting shipment, which has not happened in recent years. These are our largest pieces of machinery and our most expensive pieces of inventory. This accounts for a portion of the increase in inventory compared to the same period last year.

#### *Trends and Uncertainties*

The price of steel influences our cost of goods sold for Art's-Way Manufacturing and Art's-Way Vessels. In the past, we experienced challenges due to a sharp increase in the price of steel. We are currently seeing negative effects due to the price of steel, and continued increases may have a more significant negative impact on our cost of goods sold.

Rising fuel costs also impact our profitability. We primarily transport our finished products and incoming raw materials by truck and standard carriers; as such, diesel prices have negatively impacted our cost of goods sold in recent periods.

Similar to other farm equipment manufacturers, we are affected by items unique to the farm industry, including items such as fluctuations in farm income resulting from the change in commodity prices, crop damage caused by weather and insects, government farm programs, interest rates, and other unpredictable variables.

(iii) Liquidity and Capital Resources

Our main source of funds year-to-date came from proceeds from the line of credit, which increased by \$1,754,000 over our 2007 year end. Another source of funds is the increase of \$1,462,000 in accounts payable at August 31, 2008 compared to our 2007 year end. As of August 31, 2008, several large invoices were payable, but within terms. These invoices were related to a significant pending project at Art's-Way Scientific. A significant use of cash was the expenditures for plant and equipment, primarily due to the construction of the manufacturing facility in Dubuque, and the purchase of a plasma cutting machine in Armstrong.

The majority of cash used by operations was used for purchasing inventory. Inventories have increased significantly since November 30, 2007, up \$5,407,409. This is partially due to the dramatic increases in the price of steel seen during the first nine months of 2008. Nearly all of our inventory items at Art's-Way Manufacturing and Art's-Way Vessels are steel based. We have also increased our purchasing due to the production of items associated with the newly acquired Miller Pro product line. At August 31, 2008, our inventory of raw materials and finished goods for the Miller Pro product line is approximately \$4,033,000.

See note 6 of the notes to the consolidated condensed financial statements for a discussion of our credit facilities, as such facilities provided additional cash to finance the above mentioned items.

(b) Off Balance Sheet Arrangements

None.

Item 3

CONTROLS AND PROCEDURES

Senior management, including the Chief Executive Officer, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer concluded that our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is (a) accumulated and communicated to our management, including our Chief Executive Officer, as appropriate to allow timely decisions regarding required disclosure; and (b) recorded, processed, summarized and reported, within the time specified in the SEC's rules and forms. Since that evaluation process was completed, there have been no significant changes in our disclosure controls or in other factors that could significantly affect these controls.

There were no changes in our internal control over financial reporting, identified in connection with this evaluation that occurred during the period covered by this report that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Part II - Other Information

ITEM 1. Legal Proceedings

During the period covered by this report, we were not a party to any legal action or claim which was other than routine litigation incidental to our business.

ITEM 2. Unregistered Sales of Equity Securities

On August 21, 2008, our Executive Chairman of the Board of Directors, J. Ward McConnell, Jr., exercised options to purchase 2,000 shares of common stock which were granted under our 2007 Non-employee Directors' Stock Option Plan. The exercise price of the shares was \$12.10 per share. The total exercise price of the options was \$24,200, which was paid in cash to the company.

ITEM 3. Defaults Upon Senior Securities

None.

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

None.

ITEM 5. Other Information

None.

ITEM 6. Exhibits

See Exhibit Index on page 18 of this report.

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SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ART'S-WAY MANUFACTURING CO., INC.

By: /s/ Carrie L. Majeski  
Carrie L.Majeski  
Chief Executive  
Officer/President  
(principal executive  
and financial  
officer)

Date: October 7, 2008

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Exhibits Index

<b>Exhibit No.</b>	<b>Description</b>	<b>Method of Filing</b>
3.1	Articles of Incorporation of Art's-Way Manufacturing Co., Inc.	1
3.2	Bylaws of Art's-Way Manufacturing Co., Inc.	1
31.1	Certificate pursuant to 17 CFR 240 13(a)-14(a)	*
32.1	Certificate pursuant to 18 U.S.C. Section 1350	*

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(1) Incorporated by reference to the exhibit of the same number on our annual report on Form 10-K for the fiscal year ended August 27, 1989.

(\*) Filed herewith.

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